Income taxes in Poland: Overview

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INCOME TAXES IN POLAND: OVERVIEW

In Poland there are two types of income tax, abbreviated to PIT and CIT. These abbreviations are derived from the English names: Personal Income Tax and Corporate Income Tax, and officially appear in the abbreviated forms only in the names of tax forms. On the other hand, tax legislation refers to:

- personal income tax; and
- corporate income tax;

The first is paid by individuals. The name of the second tax could suggest that it is paid by legal persons. But the catalogue of taxable persons in CIT is much broader, but this issue we will discuss slightly later.

Income tax in its present form has existed since the early 1990s. In 1989, the Corporate Income Tax Act was adopted, which sought to unify and simplify a complicated and inefficient system of income tax on enterprises. The Act was modified in 1992. However, a breakthrough in the tax system reform came on 1 January 1992, when general personal income tax was introduced, which replaced the agricultural tax (in part related to 'special branches of agricultural production', which we will briefly discuss later on), remuneration tax, surtax and wage tax.

Basic concepts related to income taxes

Before we go into more details related to various types of income tax, we will explain some basic concepts concerning the tax.

The object of income taxes (and therefore the object of taxation) is income. Income represents the excess of revenue over expenditure.

So the common understanding is that income equals profit, or what we are left with once we deduct own expenses. On the whole, the concept is understood in the same way in tax regulations, although there are numerous provisions that often complicate the determination of income.

Example:

Mr. Smith buys a flat for 200,000 PLN. After 3 years he sells the flat for 300,000 PLN. This means that Mr. Smith earned 100,000 PLN income on the transaction (if we assume, for simplification reasons, that he has not incurred any transaction-related expenses). Income derived from sales of real property is subject to income tax; therefore, Mr. Smith will pay the tax on the amount of 100,000 PLN.

In order to determine income, we need to know both the revenue and expenditure.

Revenue consists of money and monetary assets received by or made available to the taxable person during a calendar year, as well as the value of benefits received in kind and other free performances.

This is a basic, general definition, which, depending on the source of revenue and the type of tax may be more or less different. In any case, to put it simply, revenue consists of the money and other benefits that a taxable person receives.

On the other hand, revenue expenditure consists of expenses incurred in order to obtain revenue. These expenses are subject to various regulations as well. In practice, the question which expense can or cannot be considered an expenditure item might be complicated and ambiguous. A positive difference between revenue and expenditure is income. In other words, if revenue is higher than expenditure, we deal with income.

Sometimes (especially in business activities), an opposite situation occurs, namely expenditure turns out to be higher than revenue. Then we deal with a loss. Loss means that no income has been earned and thus there will be no tax.

Example:

Mr. Jones buys a passenger car for 30,000 PLN. After 5 months he sells the car for 25,000 PLN. Because the transaction revenue (25,000 PLN) is lower than the expenditure (30,000 PLN), Mr. Jones records a loss of 5000 PLN on the transaction. Therefore, the car sales transaction will not be taxed.

According to Income Tax Acts, a loss recorded in a given year may be deducted from taxable income in subsequent years, on the proviso that the loss can only be deducted over the period of 5 consecutive years, and that a single annual deduction must not exceed 50% of the entire loss.

Example:

Anna pursues a business activity. In 2008 her business records a loss of 10,000 PLN. In 2008 she does not pay the tax. In 2009 her business earns 50,000 PLN income. She can use that income to reduce her business loss from the previous year; however, the loss deduction must not exceed 50%, so she may deduct up to 5000 PLN.

So Anna deducts the amount, and thus her taxable income in 2009 amounts to 45,000 PLN. She can deduct the remainder of the loss (5000 PLN) over the next 4 years.

Taxation of revenue

As a general rule in the income tax regime, taxation is applied to income. But tax regulations also allow for situations where it is revenue rather than income that is taxable. One might ask why? After all, revenue is almost always higher than income (in real life it is rather unlikely to earn revenue without incurring some expenditure), which means that we pay the tax on a higher taxable base.

But it makes sense somehow. Firstly, rates of taxes on revenue tend to be lower. Secondly, revenue is easier to determine compared to income (as we do not have to establish expenditure). Therefore, lump-sum taxes are aimed at simplifying the settlements with tax authorities. For this reason, revenue taxation is often referred to as lump-sum taxation.

Example:

Trevor is engaged in a clothing trade business. In 2012 he earns sales revenue of 100,000 PLN and incurs expenditure of 70,000 PLN. Thus, Trevor earns income of 30,000 PLN.

For simplicity reasons, let us assume that at the beginning of 2012 Trevor could choose between two taxation schemes for his business activities, namely income taxation at the rate of 19% or revenue taxation at the rate of 3.5%.

Within the income taxation scheme, Trevor will pay: 30,000 PLN x 19% = 5700 PLN.

Within the revenue taxation scheme, Trevor does not have to bother about expenditure, and can pay less tax because of the lower tax rate:

100,000 PLN x 3.5% = 3500 PLN.

In our example, the lump-sum tax calculated on revenue is more advantageous. Not only was it easier for us to calculate the taxable base, but also the tax calculated turned out to be lower.

Of course, the lump-sum tax on revenue will not always be more advantageous. Moreover, a taxable person is free to choose the form of taxation in some situations only. The lump-sum tax is in fact an exception to the rule, which is to tax all income.

It is worth mentioning here another concept related to taxes in general, and to income taxes in particular, namely the taxable base.

Colloquially speaking, the taxable base is what we pay the tax on. It is therefore an expression of the object of taxation in terms of value or quantity.

In income taxes, the taxable base consists of income or revenue, and this base is expressed as money. In the case of the lump-sum tax (i.e. the tax paid by the clergy), the taxable basis may be the number of inhabitants (of a parish or a locality).

For some other taxes, the taxable base can be expressed in a different unit of measurement, such as square metres, cubic centimetres, litres, pieces, quintals or hectares.

Another important tax concept in general, and for income taxes in particular is the tax rate. The tax rate is a figure that in conjunction with the taxable base makes it possible to specify the tax amount. In income taxes, tax rates may be fixed or variable.

In the case of a fixed rate, the tax amount increases in proportion to changes in the amount that is subject to the tax (the rate is also known as a proportionate or flat rate).

In Poland, variable rates are progressive, which means that the amount of taxes increases with the increase of the taxable base.

The tax rate is expressed as a percentage or an amount.

Flat rate

Taxable persons in corporate income tax pay the tax according to the flat rate of 19%. It means that no matter what the taxable base (i.e. the amount of income); their tax will always be 19% of the base.

Variable (progressive) rate

As a rule, individuals pay the tax according to a progressive variable rate.

2013, 2014

Basis for calculation		The tax will amount to
more than	up to	
	85,528	18% minus 556.02 PLN of the tax credit
85,528		14,839.02 PLN + 32% on the excess over 85,528 PLN

A progressive income tax rate means that the tax rate will soar once a specific threshold is exceeded. In the currently applicable framework of taxable bands, income of up to 85,528 PLN is taxed at the rate of 18% minus 556.02 PLN. The excess over the threshold is taxed at the rate of 32%.

Example:

A taxable person who earns income of 80,000 PLN pays the tax of:

80,000 PLN x 18% – 556.02 PLN = 13,844 PLN (the tax is rounded off to the nearest whole zloty).

The real tax rate is therefore: 13,844 PLN / 80,000 PLN x 100 = 17.31% (rounded to two decimal places).

A taxable person who earns income of 88,000 PLN pays the tax of:

14,839.02 PLN + 2472 PLN x 32% = 15,630 PLN.

The real tax rate is therefore: 15,630 PLN / 88,000 PLN x 100 = 17.76%.

With an increase in income from 80,000 PLN to 88,000 PLN, the tax rate increases by 2.60%.

This is what we call progressive taxable bands.

With the amount-based rate we deal in lump-sum taxes.

Example:

A parish priest in a parish with less than 1000 inhabitants pays a quarterly tax amount of 416 PLN.

A taxable person in income tax

While trying to define the tax concept with our own words, we will find out that the two most important criteria for the definition are: the object and the subject of taxation.

In income tax, the object of taxation is income, as we have already mentioned. Exceptionally, the object of taxation may be revenue or the size of a locality or a parish.

On the other hand, the subject of taxation is a party responsible for payment of the tax. Simply put:

- taxable persons in income tax are parties that have earned income, and are therefore obliged to pay income tax. They may be individuals, legal persons and non-corporate bodies, which are obliged to pay the tax in accordance with legal regulations.

An individual is any person from the moment of birth.

A legal person is an organisational unit which may be the subject of rights and obligations under civil law. The fact of having a legal personality stems either directly from the Act (e.g. Article 33 § 1 of the Civil Code), or from the fact that an entity is entered into the register (e.g. Article 12 of the Code of Commercial Companies dealing with corporations).

The concept of other non-corporate body is not defined in the legal regulations. These include, for example, partnerships and other entities, which are considered taxable persons by legal regulations.

As we know, a taxable person is obliged to pay the tax. The tax is paid to a tax authority, usually a tax office.

With income tax it is often the case that tax calculations and payments are handled not by a taxable person on their own but by an intermediary known as a tax payer.

Example:

A person who derives their income from employment does not actually pay income tax on their own. Instead, their employer acts as a taxpayer, i.e. it is obliged to calculate the tax, collect it from the taxable person (the employee) and pay it promptly to a tax authority.

The taxable person is only obliged to submit an annual tax return in which they will disclose the income earned and the tax collected by the taxpayer (specifically: tax advances). Most frequently, the sum of tax advances corresponds to the annual tax, so a taxable person does not have to pay any extra amounts (though sometimes it may be necessary to supplement the tax, for example, when several sources of income exist, or when income is earned from abroad). Sometimes a taxable person who benefits from tax reliefs may recognise an overpaid tax in their annual return.

In some cases, a taxable person may be relieved from the obligation to file an annual tax return by the taxpayer (the employer) or by, for instance, the Social Insurance Institution (ZUS).

Taxation of income of individuals and legal persons

Earning means taxes. This general rule means that any entity that earns income is a taxable person in the income tax regime (with such entities including individuals, legal persons and other bodies). An exception to this rule may apply if a taxable person chooses the lump-sum taxation scheme:

then, even though a taxable persons has not earned income, they will have to pay the tax just because they earned some revenue (and such situations should also be borne in mind when one opts for lump-sum forms of taxation).

Example:

Let us assume that Trevor, whom we mentioned before, is engaged in a clothing trade business and earns in 2012 the sales revenue of 100,000 PLN but incurs expenditure of 120,000 PLN. By the same token, then, Trevor records a loss of 20,000 PLN.

If Trevor opted to pay income tax (within the general scheme), they would not have to pay any tax. If, however, he chose the lump-sum taxation, he would have to pay the tax of 3500 PLN anyway (even though he suffered a loss).

Taxable persons' income (revenue) may be subject to taxation in accordance with the provisions of:

- Personal Income Tax Act of 26 July 1991;
- Act of 20 November 1998 on the Lump-sum Income Tax on Certain Revenue Earned by Individuals;
- Corporate Income Tax Act of 15 February 1992;
- Act of 24 August 2006 on Tonnage Tax.

Personal income tax

The universal nature of personal income tax is expressed both subjectively, which means that the tax is levied, in principle, on all individuals, and objectively, which means that the tax is paid on all types of income that may be obtained by an individual.

So in the Personal Income Tax Act (which was amended more than 200 times over 21 years), we find regulations concerning income derived from:

a) employment;
b) civil law agreements;
c) business activity (self-employment of individuals);
d) special branches of agricultural production;
e) rental;
f) capital gains and property rights;
g) sales of real and other property;
h) other sources.

Any person who earns income from any of the above-listed sources becomes a taxable person. And as we become an individual from the moment of birth, taxable persons in income tax are also children who earn income (e.g. from their own work or based on orders); however, in the case of minors, annual returns on children's behalf are submitted by their parents).

The catalogue of taxable income items is thus, as we can see, a very broad and open one. This is because of the fact that the legislator has reserved for itself the right to tax "other sources of income", which sometimes inspires the tax authorities to quite absurd ideas, such as the taxation of neighbourly help.

Example:

According to a lunatic idea of the tax authorities, if a neighbour gives us a morning lift to work in his car, we obtain income (because we have not had to spend ten or so zloty on a ticket), and such income should be taxed.

Although it may sound ridiculous, the idea is in fact justified under the Personal Income Tax Act.

The only income items that are certainly not subject to personal income tax are those expressly excluded from taxation by the Act itself, namely:

- from agricultural activities, with the exception of revenue from special branches of agricultural production – agricultural activities are subject to agricultural tax instead;
- from forest management within the meaning of the Act on Forests and the Act on the Allocation of Agricultural Land for Afforestation – the activity is subject to forest tax instead;
- subject to the provisions on inheritance and donations tax;
- from transactions that may not be the subject of legally binding agreements (in general, this exclusion means that income derived from crime must not be taxed);
- resulting from the division of joint property of husband and wife resulting from cessation or limitation of the joint property regime, and revenue from a distributive award following the cessation of a system of separate estates in matrimony, or the death of one of the spouses;
- of a ship owner that is taxed pursuant to the Act of 24 August 2006 on Tonnage Tax;
- from benefits related to married life referred to in Article 27 of the Family and Guardianship Code, which are covered by joint property of husband and wife.

The last item on the list above means "intra-familial benefits". So, as we have mentioned before, a tax authority is entitled to demand the tax on "income" resulting from the use of a lift to work, but not if the lift was given by a spouse.

Limited and unlimited tax obligation

The universal nature of personal income tax is also reflected in the 'unlimited tax obligation'. This obligation means that a person who lives in Poland cannot escape the tax. So even if we leave the country to work abroad, the Polish tax authorities will still be interested in our foreign earnings. This is because of the fact that a person whose place of residence is Poland is subject to the tax in Poland on their entire income, regardless of whether it has been earned in Poland or in another country. The same applies to foreigners who live or earn their income in Poland.

However, if we earn money abroad, an issue of eliminating double taxation will occur because foreign income of persons living in Poland will attract both the Polish tax authorities and the tax authorities in the country where such income is earned.

However, as we have as already mentioned, personal income tax does not apply only to persons who live in Poland. Taxable persons will also be those who earn money in Poland. Here we deal with the 'limited tax obligation'.

Example:

Karl lives in Chotěbuz (Czech Republic) and works in Cieszyn (Poland). Because he earns income in the territory of Poland, his corresponding income is taxable in Poland too – pursuant to the Polish tax regulations (but also according to the Polish-Czech double taxation convention).

So the unlimited tax obligation means that if a person lives in Poland, their entire income earned during the year, including foreign income, is taxable in Poland.

In contrast, the limited tax obligation means that a person who earns money in Poland, although they do not live here, will pay the tax on income earned in Poland.

So it may turn out that taxable persons subject to income tax in Poland are more numerous than the total population.

The object of personal income tax consists of income, and if a taxable person derives their income from more than one source, the object of taxation in a given tax year is the sum total of income from all sources of revenue. This principle is not applied to income (revenue) that is taxed in the lump-sum scheme, and business income subject to the flat-rate tax, capital gains income and income derived from property rights and sales of real property – such income is taxed separately.

Annual tax settlement

Following the end of a tax year (for individuals the tax year corresponds to the calendar year)

– by 30 April of the following year (if that day falls on a Saturday or Sunday, the last day of the period should be the day following the holiday(s)) – taxable persons subject to personal income tax are required to file with a tax office the tax return(s), stating the amount of income earned (loss incurred) in a tax year.

30 April is also the deadline for payment of the tax amount stemming from an annual return.

Lump-sum income tax

The Act of 20 November 1998 on the Lump-sum Income Tax on Certain Revenue Earned by Individuals regulates taxation of certain revenue (income) earned by individuals:

a) involved in non-agricultural business activities;
b) earning revenue from rental, subletting, lease, sublease or other contracts of a similar nature, provided that such contracts are not concluded as part of non-agricultural business activities;
c) clergymen.

The Act distinguishes three forms of the tax:

1) lump-sum amount on registered revenue that is available to persons who derive their revenue from a business activity or rental;
2) "tax card" scheme available to certain entrepreneurs;
3) lump-sum income tax on revenue earned by the clergy, paid by clergymen.

For individuals who pursue a business activity, or derive their income from rental, a general rule is taxation with personal income tax. However, if they satisfy certain conditions specified in the Lump-sum Tax Act, they may declare their intent to pay the lump-sum tax.

In the case of the clergy, we deal with the opposite situation: in principle, they are subject to the lump-sum tax, but if they want to, they can waive that right and pay personal income tax.

Lump-sum amount on registered revenue

The lump-sum tax on registered revenue is paid on individuals' revenue from non-agricultural business activities, including the activities in the form of a civil partnership of individuals and in the form of a general partnership of individuals.

The lump-sum tax on registered revenue may be paid by taxable persons who start a business activity and opt for this taxation scheme, and if they were active in business in the preceding year – provided that their last year's business revenue did not exceed the equivalent of 150,000 EUR.

Example:

In 2012 Rob took up a trading business.

Because he wanted to pay the lump-sum tax on registered revenue, prior to the start of business activities he notified his intent to the head of a tax office (if no such notification had been submitted, he would have been subject to personal income tax in the general scheme).

The Act provides for 5 tax rates (3%, 5.5%, 8.5%, 17% and 20%), depending on the type of business.

The taxable base is revenue (not reduced by revenue expenditure).

Taxable persons that use this taxation scheme are obliged to keep: the records of revenue for each tax year separately, the equipment records, and the register of fixed and intangible assets.

Some types of businesses cannot use the lump-sum taxation scheme (including pharmacies, businesses buying and selling foreign exchange, or businesses trading in parts and accessories for motor vehicles).

As regards settlement and reporting obligations, taxable persons are obliged to calculate and pay the tax at monthly or quarterly intervals, and file an annual tax return at the end of the year (by 31 January).

Fixed-amount tax ("tax card")

This is by far the simplest form of taxation available to taxable persons engaged in some forms of business activity (mainly small-scale craftsmen).

A taxable person using the "tax card" scheme receives from the head of a tax office a decision stating a monthly amount of the tax (depending primarily on the type of activity, the size of the locality in which the business is conducted, and the number of employees).

Taxable persons in the "tax card" scheme are exempt from the obligation of bookkeeping, filing tax returns and paying income tax advances.

Corporate income tax

Entities having legal personality (primarily corporations: limited liability companies and joint stock companies) are taxable persons in corporate income tax.

In addition to legal persons, the following entities are also subject to the tax:

- non-corporate bodies, with the exception of companies without legal personality (i.e. partnerships), except that corporations in the process of formation are taxable persons;
- tax capital groups (groups consisting of at least two corporations having legal personality which are linked by capital and satisfy the conditions specified in the Act);
- companies without legal personality having their registered office or management in another state, if pursuant to the tax regulations of that state they are treated as legal persons and are taxable on their entire income in that state, regardless of where such income is earned.

Taxable persons in corporate income tax pay the tax on income, i.e. the excess of revenue over expenditure. In the case of certain revenue (e.g. dividend), the object of taxation is revenue.

The tax rate is 19% and at the end of each year taxable persons are required to submit their annual tax returns.

Tonnage tax

This tax is of the least importance for the budget. The tax is paid by shipping companies operating marine commercial vessels in international shipping.

The taxable base is income, which is determined in a rather peculiar way.

The taxable base in tonnage tax consists of a shipping company's income that corresponds to the product of: the daily rate (dependent on the net register tonnage of the ship) and the period of service in a given month of all ships operated by the company the income from which is subject to tonnage tax.

The tonnage tax is 19% of the taxable base and is paid for monthly periods.

Shipping companies are obliged to file with a tax office their tonnage tax returns, stating the tax due for a given tax year by 31 January of the following year.

Corporate Income Tax

Here we discuss some basic concepts related to the Corporate Income Tax Act: the object of taxation and taxable entities. We will examine carefully revenue: sources of, exclusions from and how its amount is determined.

It should be noted that both Income Tax Acts, i.e. Corporate Income Tax Act and Personal Income Tax Act, are similar or even identical in many respects concerning the taxation of business activities. So both Income Tax Acts contain many provisions whose wording is very similar or even the same when it comes to revenue, expenditure or methods by which income is determined.

Taxable persons in corporate income tax

The concept of "legal persons" in the context of income tax is a slight simplification, because the catalogue of taxable persons for this tax is much wider.

So let us see what entities may be taxable persons for corporate income tax purposes.

The Corporate Income Tax Act mentions the following entities as taxable persons:

a) legal persons;
b) non-corporate bodies, with the exception of companies without legal personality, except that corporations in the process of formation are taxable persons;
c) tax capital groups (groups consisting of at least two corporations having legal personality which are linked by capital and satisfy the conditions specified in the Act);
d) companies without legal personality having their registered office or management in another state, if pursuant to the tax regulations of that state they are treated as legal persons and are taxable on their entire income in that state, regardless of where such income is earned.

A legal person is an organisational unit which may be the subject of rights and obligations under civil law. The fact of having a legal personality stems either directly from the Act (e.g. Article 33 § 1 of the Civil Code), or from the fact that an entity is entered into the register (e.g. Article 12 of the Code of Commercial Companies dealing with corporations).

The concept of other non-corporate body is not defined in the Act. Such general wording allows the conclusion that taxable persons in corporate income tax are all organisational units unless specifically excluded. Hence, taxable persons are companies without legal personality, i.e. partnerships: civil partnerships, general partnerships, limited liability partnerships, limited partnerships and limited partnerships on shares. However, things will change in the case of limited liability partnerships on shares, which starting from 2014 will be incorporated into the circle of corporate income tax payers.

Examples of organisational units that are (or may be) taxable persons in corporate income tax include: housing communities, associations and campaign teams.

An interesting "form" of a taxable person is a tax capital group. A group comprising at least two corporations may become one entity for income tax purposes. A tax group pays advance income tax and the annual tax, which is the difference between the total income and the total loss of individual entities within the group. The main tax benefit resulting from the establishment of a tax capital group is the possibility to cover the losses of one group company as they arise with income earned in a given tax year by another company in the same group.

Example:

Three corporations having legal personality form a tax capital group.

The companies achieve the following income from their business operations: Company X – income of 40,000 PLN, Company Z – income of 60,000 PLN; Company Y – loss of 20,000 PLN.

In a tax capital group framework, a taxable base is determined by reference to the concept of aggregate income and deduction of total losses. So the total income of the tax capital group is 80,000 PLN (40,000 PLN + 60,000 PLN - 20,000 PLN).

The tax capital group's tax liability for the tax year concerned is 15,200 PLN (80,000 PLN x 19%). If each company operated individually, their respective tax liabilities would be:

- tax payable by Company X: 7600 PLN (40,000 PLN x 19 %);
- tax payable by Company Z: 11,400 PLN (60,000 PLN x 19%);
- whereas Company Y would have the right to settle its loss over the next 5 tax years.

If the Companies X, Y and Z operate as a tax capital group, they will pay the total tax of 15,200 PLN. On the other hand, if they operate individually, their tax liability will amount to 19,000 PLN

The above example shows that establishment of a tax capital group is economically justified if at least one member company generates losses, because such losses can be covered with the current gains of the remaining companies.

Unfortunately, legal regulations impose a number of obligations on entities wishing to create a tax capital group. That is why it is not a popular arrangement. Companies that intend to create a group must, among other things, have average per-company equity of at least 1,000,000 PLN, while one of the group companies (the parent company) should have at least a 95% share in the capital of each of the remaining companies. In addition, such companies must not have any arrears with their payments towards the budget. Moreover, the group must throughout its life (at least 3 years) earn income whose share in revenue is not lower than 3%.

The Act also indicates that the group of taxable persons can include foreign companies, which admittedly do not have a legal personality, but pursuant to tax regulations in their country of origin are treated as legal persons and are taxable on their entire income in that state, regardless of where such income is earned.

An example of such entity may be a German limited partnership on shares (in German: Kommanditgesellschaft auf Aktien). Pursuant to the German legislation it is treated as a corporation, so in spite of the fact that in Poland limited partnerships on shares (S.K.A.) are not taxable persons in CIT (although only until the end of 2013), a German KGaA operating in Poland will be subject to corporate income tax.

Related parties

A special type of taxable person includes related parties, i.e. the entities linked by capital or personal ties. Related parties may not exploit the existing ties to reduce their taxable income. In practice, this means that such entities must cooperate on an arm's-length basis. If they do not follow the above requirements, then a tax authority will be authorised to levy tax based on income estimation (Article 11 of the CIT Act).

Example:

Two limited liability companies JON and JIM are related parties. JON sells office supplies to JIM. Sales in 2012 amount to 50,000 PLN. At the end of the year, JON records a loss of 100,000 PLN, while JIM makes a profit of 100,000 PLN. As a result, JON will not pay any tax (because it has recorded a loss), and JIM will pay 19,000 PLN in tax.

Related entities often feel the temptation to exploit the links in order to reduce tax. Since in our example, JON's loss is big, no tax will apply even if the loss is reduced, but JIM will be able to reduce its taxable income in this way.

Therefore, the companies agree that instead of selling goods at the price of 50,000 PLN, they will set the price at 70,000 PLN. In this way, JON's revenue increases by 20,000 PLN, and JIM's expenditure is higher by 20,000 PLN. As a result, JON's loss becomes reduced to 80,000 PLN (so still does not have to pay the tax), whereas JIM's profit will amount to 80,000 PLN, so will pay the tax of 15,200 PLN. By exploiting the inter-company links, JIM manages to save 3800 PLN on tax.

For the state budget, such cooperation, involving the use of inter-company links in order to reduce income and tax, is a harmful arrangement. Therefore, tax authorities try to prevent it by verifying whether the terms of cooperation between related parties do not deviate from the arm's-length principle.

Related parties are obliged to draw up special tax documentation for their transactions (Article 9a of the CIT Act) – for the tax authorities, this documentation constitutes proof that the terms of cooperation (usually the price) between related parties are not affected by the existing inter-company links.

If a taxable person fails to submit such documentation of transactions to tax authorities, and the ensuing tax proceedings prove that the terms of transactions established or imposed differ from those which would apply between independent entities, and as a result the taxable person does not disclose income or discloses income lower than should be expected, then the higher income/lower loss will be established (compared to the figure declared by the taxable person). The difference between the income declared by the taxable person and that established by tax authorities is taxed at the rate of 50% (Article 19 para. 4 of the CIT Act).

Tax-exempt entities

As mentioned above, the Act seeks to tax every possible entity that earns income. However, the law provides for certain exemptions for some public finance entities. These include the State Treasury, the National Bank of Poland (NBP), earmarked funds, the Social Insurance Institution (ZUS) and pension funds. These entities exist outside the tax legislation framework, and as such are not obliged to file tax returns.

Non-taxable revenue

The provisions of the Corporate Income Tax Act do not apply to:

1) revenue from agricultural activities, with the exception of special branches of agricultural production;
2) revenue from forest management;
3) revenue from transactions that may not be the subject of legally binding agreements (e.g. crime, bribes);
4) revenue of a ship-owner that is subject to tonnage tax.

Unlimited and limited tax obligation

As in the case of individuals, the legislation defines the scope of tax obligations for legal persons depending on the residence of the taxable person.

Legal persons (and other entities) that have their registered office (or management based) in Poland, are taxed on their entire income, regardless of where it is earned (unlimited tax obligation).

In contrast, entities that do not have a registered office or management in Poland are taxed in Poland only on that part of their income that they earn within Polish territory (limited tax obligation).

The concept of a registered office is defined in the Civil Code and, unless there is a specific provision to the contrary, a legal person's registered office is understood as the place where its governing body is established.

Tax year

While discussing corporate income tax, it is also worth mentioning that sometimes a tax year is not synonymous with the calendar year. Indeed, a tax year can sometimes last longer than 12 months.

A general rule specified in the Tax Code is that the tax year corresponds to the calendar year, unless a specific tax law provides otherwise. And the Corporate Income Tax Act is precisely the only exception and does provide otherwise. Pursuant to the Act, a taxable person has the right to adopt a different tax year as long as it lasts 12 months.

Changes in the "tax calendar" result in a "transition year" of more than 12 months (though it must not last longer than 23 months).

Example:

A company whose tax year to date has corresponded to a calendar year adopts a resolution that the tax year should now be the period of 12 consecutive months between 1 June and 31 May. Once the "old" tax year ends, i.e. after 31 December, the company will have one month to notify the head of the tax office of the change.

Then the new tax year will last between the end of the "old" tax year and the end of the "new" one. So in the example, it will be the period between 1 January of that year and 31 May of the following year (17 months). The next tax year will last the "prescribed" 12 months, i.e. from 1 June to 31 May.

Changes in the tax year may be related to the periodicity of income earning, or a desire to extend the period in which the tax loss can be deducted.

Example:

For Company X, the tax year corresponds to the calendar year. In 2007, the company incurs a loss of 550,000 PLN. Because over the next few years, the company earns a fixed income of 100,000 PLN/year, it is able to deduct 400,000 of the loss in the years 2009-2012.

In 2013, the company plans to earn income of 100,000 PLN. This means that it will be unable to deduct 50,000 PLN of the loss (similarly to personal income tax, under corporate income tax arrangements, the loss may be deducted over the period of 5 consecutive years, and an annual deduction must not exceed 50% of the entire loss amount).

In this situation, the optimization solution will be the decision to change the tax year and assume that it will last, say, from 1 December to 30 November. Thus, the first year after the change (and at the same time the fifth year in which the loss could be deducted for the last time) will run from 1 January 2013 to 30 November 2014, or 23 months. This period should be sufficient for the company to achieve income of at least 150,000 PLN and thus deduct the remainder of the loss.

Object of taxation in corporate income tax

According to the general principles, an object of taxation in corporate income tax consists of income, regardless of the source of revenue from which such income is derived.

Income is the excess of total revenue over revenue expenditure, as earned in a tax year. If revenue expenditure exceeds the total revenue, then the resulting difference is a loss.

Like with personal income tax, if a taxable person records a loss in a tax year, they can reduce their income with the loss amount over the following consecutive 5 tax years, provided that no single annual deduction exceeds 50% of the entire loss amount (Article 7 of the CIT Act).

For revenue derived from interest in profit of legal persons (such as dividend) and revenue of foreign entities related to intangible services (e.g. interest, royalties, copyright, or consulting) – the object of taxation is revenue (Article 10 and 21 of the CIT Act).

Revenue

In fact, the Corporate Income Tax Act does not give a definition of revenue.

The regulations only specify types of revenue – by means of a list of examples contained in Article 12; moreover, they specify an exhaustive list of types of a business entity's cash inflows that are not considered revenue.

Let us have a look at the most popular forms of revenue that are mentioned in the Act.

Money and monetary assets received

A general rule in the case of monetary revenue is that it must be "received". A taxable person receives money when it becomes part of their property.

Within the meaning of the Act, money is also considered received when it becomes available to a taxable person, e.g. when it is credited to the person's bank account.

Value of property or rights received free or charge or partially paid, and the value of other free-of-charge or partially paid performances

As in the case of individuals, free-of-charge performances received by legal persons may be considered revenue. Any benefit received by a taxable person free of charge may constitute revenue for tax purposes. And as with individuals, this issue is controversial and results in conflicting interpretations and judgments in the legal person domain.

An example of a controversial "performance" is granting a free-of-charge guaranty for a loan taken out by the company by a shareholder in that corporation.

Taxable persons claim that it is difficult to speak here of any performance at all, given that a shareholder does not incur any expenditure, and does not provide any special labour input in connection with the guaranty. Although some tax authorities and administrative courts agree with this approach, the Ministry of Finance expresses a "dissenting opinion" on this issue, and in its general interpretation (which serves as “ministerial recommendations” for tax authorities) states that the use of such guaranty by the company is actually revenue.

According to tax authorities, free-of-charge performances for companies also include resignation from remuneration by a board member or other persons performing any services for the company. So in this situation, a free-of-charge performance is doubly disadvantageous to taxable persons.

Example:

A member of the board resigns from remuneration. How does this fact affect the amount of tax paid by a company?

Suppose that in a tax year the company's revenue is 1,000,000 PLN, and its expenditure is 400,000 PLN. Average remuneration of board members in similar companies approximates to 100,000 PLN/year.

If the company actually paid such remuneration to the board member, it would be the company's expenditure item, which would increase its total expenditure. Consequently, corporate income for the tax year would amount to 500,000 PLN, which at the current CIT rate of 19% would mean a tax of 95,000 PLN.

Resignation from remuneration by a board member is a free-of-charge performance for the company's benefit.

In the situation described here, expenditure remains at the actual level of 400,000 PLN, but the value of the performance concerned increases the company revenue so that it amounts to 1,100,000 PLN. Thus, the company income amounts to 700,000 PLN, and its income tax is 133,000 PLN.

Although the company saved 100,000 PLN on the remuneration concerned, its tax increased by 38,000 PLN. Therefore, the real benefit for the company amounted to 62,000 PLN. Actually, we can say that by having resigned from their due remuneration, the board member has done the greatest favour to... the tax authorities.

The rules for determining the value of free-of-charge performances in the regime of corporate income tax are akin to those for personal income tax:

- if a performance is related to services falling within the scope of a performing entity's business activity – the value is established based on the prices charged to other customers;
- if a performance is related to services purchased – the value is established based on purchase prices;
- if a performance consists of the provision of premises – the value will be an equivalent of the rent that would be payable if a rental agreement was concluded for the premises;
- in other cases the value is established based on market prices charged for the provision of services or property or rights of the same kind and type, taking particularly into account their condition and wear, and the time and location when and where they are made available.

The value of partially paid performance that are considered a taxable person's revenue is the difference between the value of such performances, as determined in accordance with the above-mentioned principles, and the fee paid by the taxable person.

Value of written-off or time-barred liabilities (including borrowing liabilities)

An interesting type of performance which constitutes tax revenue is writing-off of liabilities, including interest on borrowings.

For a lender, interest is revenue when received. So, if no interest is received, even if the fact results from writing off the item by the lender, no tax consequences occur.

On the other hand, interest written-off becomes the borrower's revenue under the concept of a free-of-charge performance. This is because the borrowing company has been released from the obligation to pay.

Example:

A company obtains a borrowing on which it should pay 10,000 PLN interest in 2012. The lender remits the interest. For the borrower, interest remittance translates into the higher income tax. If the company paid 10,000 PLN interest, its tax would be lower by 1900 PLN.

On the contrary, the performance received increases the tax by 1900 PLN. By the same token, the company will be required to pay 38% more in tax. Just as in the previous example, the remittance of 100,000 PLN in interest translates into the company's real benefit of 6200 PLN.

3800 PLN is the tax authorities' gain.

So we cannot overlook the fact that when a company does not pay due interest on time (even for many years), its position will be better than if the interest was remitted.

Value of claims returned that have previously been written down as uncollectible or written off and recognised under revenue expenditure

It may happen that a debtor does not pay. In the business activity domain, revenue consists of (to be discussed in a little while) performances that are due, even if they have not been received. So even though we have not received payment, we have to pay the tax on any revenue that is due.

The tax regulations, however, provide for some leeway to "compensate" for the tax loss resulting from the debtor's insolvency. Once relevant conditions are satisfied, unrecovered debt may be recognised under revenue expenditure and thus reduce the tax amount.

If, however, after the recognition of debt under revenue expenditure, the outstanding amount is recovered, then the revenue should be disclosed again as revenue.

Example:

Company X provides a service to Fraudstery PLC and issues a corresponding invoice for 10,000 PLN. It recognises the amount as revenue and pays the tax due on that amount (let us assume that it is 1900 PLN).

Unfortunately, in spite of intensive debt collection efforts, the amount has not been recovered. So Company X recognises the uncollected claim under expenditure and thus reduces the tax due (by the same 1900 PLN).

If, however, Fraudstery PLC returns the debt, Company X will have to recognise revenue again.

Revenue in foreign currencies

In corporate income tax, revenue in foreign currencies is converted into PLN according to the same rules as in personal income tax, i.e. according to the average FX rate announced by the National Bank of Poland, as applicable on the last working day preceding the revenue day.

Revenue from business activities

As a general rule, revenue in the income tax regime consists of a performance received.

This rule, however, does not apply to business activities. Revenue related to business activities and special branches of agricultural production is understood as revenue that is due, even if not actually received, less the value of goods returned, and the rebates and cash discounts granted.

So in business activities, the revenue day is the day when a receivable originated rather than the day when a taxable person received money for the product sold or the service rendered. This solution can lead to a situation in which a taxable person has not received any payment from their contractor, but will still be obliged to pay income tax. Here we deal with the principle known as the accrual principle.

With respect to business revenue, the accrual principle does not apply to revenue in the form of interest on borrowings granted, cash at bank and contractual indemnities received, as they are all governed by the cash-basis principle (revenue is generated only upon receipt of the performances concerned).

Rebates and cash discounts are price reductions. A rebate is granted based on the subject (for specific customer categories), the object (e.g. form of sales), or in connection with actual or anticipated damage suffered by a counterparty (e.g. in connection with sales of lower grade or defective products).

Cash discount applies when payment occurs in the form that is more convenient for the seller, e.g. in cash or at an earlier date than the date specified in the contract.

Revenue day in business activities

The revenue day in business activities is understood as the day when goods are delivered, a property right is disposed of, or a service is rendered or partially rendered but not later than:

- the invoice day; or
- the day of payment of the amount due.

Example:

Company A sells goods on 30 April (and releases them on the same day). A corresponding invoice is issued on 3 May. Revenue is generated in April (goods release date).

Company B completes a transport service on 27 February, and issues a corresponding invoice on 15 March.

Revenue is generated in February (service performance date).

If the parties agree that the service should be settled in billing periods, then the revenue day shall be the last day of the billing period specified in the contract or on the invoice, and should fall at least once a year (this provision applies as appropriate to electricity, heat and network gas supplies).

In practice, providers of company services may freely establish the revenue day (provided that at least one such day is designated during a year).

Example:

A company rents out commercial premises starting from 1 January. The agreement assumes that the parties will make settlements on a quarterly basis, and invoices will be issued on the last day of the quarter. What will be the revenue day?

In accordance with the legislative provisions, the revenue will be generated not later than on the invoice day or the day of payment of the amount due. Since in our example the settlements will be quarterly and the amount due will be paid once the invoice is issued, the revenue day will fall on the invoice day.

Revenue from transfer of property or property rights for consideration

In the case of sales, revenue consists of the price. However, if the price is significantly and unreasonably divergent from the market value of the property or rights, then a tax authority determines the revenue at market value. This means that the tax authority may issue a decision in which it determines revenue that is different (obviously higher) than the price-based revenue.

Market value of property or property rights is established based on market prices charged in trading in property or rights of the same kind and type, taking particularly into account their condition and wear, and the time and location when and where they are transferred for consideration.

In a situation where a tax authority finds that the price indicated in the contract is significantly divergent from the market price of property or rights, it will, in the first place, request all parties to the contract to change the value or indicate reasons for having stated a price that is significantly divergent from the market value.

If the parties do not comply with that request (i.e. they fail to respond, change the value, or indicate reasons for having stated the price that is significantly divergent from the market value), then the tax authority will establish the value taking into account an opinion of an expert or experts. If the value determined in this way differs by at least 33% from the value expressed as the price, the cost of such opinion of an expert or experts will be borne by the transferring party.

Exemptions from revenue

The CIT Act also lists categories that are not classified under tax revenue (Article 12 para. 4 of the Act). The following items are excluded from revenue (non-exhaustive list):

- payments collected or accrued receivables relative to supplies of goods and services that will be performed in subsequent reporting periods;

So advances on supplies of products or services are not considered revenue.

- accrued but not received interest on receivables, including on borrowings (loans) granted;

Even if interest is related to business activities, for such interest we do not apply the accrual basis but the cash-basis principle. In other words, revenue does not originate just because interest is due: it must be actually received by a taxable person.

- refunded, redeemed or abandoned taxes and charges which constitute income of the state budget or local government budgets, not recognised under revenue expenditure;
- other reimbursed expenses, not recognised under revenue expenditure.

Both of these categories are a practical expression of a general rule that if a taxable person receives a refund of any performances that they have not originally recognised under revenue expenditure, then the refund will not be revenue either.

Example:

Revenue expenditure may not include, for example, income tax. So a tax refund (if any) will not be considered revenue either.

- the amount of interest received in connection with the refund of overpaid tax liabilities and other budgetary dues, as well as interest on the refunded difference in tax on goods and services, as defined in separate regulations;

On the whole, overpaid tax does not bear interest. However, if a tax authority fails to complete the refund within the time limit specified in legal regulations, then the refund bears interest.

Such interest, however, will not be the taxable person's revenue.

- value of performances provided by volunteers on the conditions specified in regulations governing activities in the public interest and volunteerism.

We have already mentioned that a free-of-charge performance for the benefit of taxable persons creates revenue. However, such revenue does not originate if performances are provided by volunteers.

Revenue in personal income tax

Pursuant to a general rule, individuals pay tax on the total income earned in a given year. In other words, we reduce revenue from various sources by expenditure that relates to the revenue, and work out the sum total of income. Then we calculate income tax on the total income according to the existing taxable bands. This method for determining the total income also involves the constraint that a loss associated with one source of income must not reduce the overall income.

Example:

In 2012 Rob's revenue and expenditure was as follows:

- revenue from copyright: 20,000 PLN, expenditure: 10,000 PLN;
- revenue from dependent personal services: 31,500 PLN, expenditure: 1500 PLN;
- revenue from business activities: 30,000 PLN, expenditure: 40,000 PLN.

So Rob obtained the following income from individual sources of revenue:

- copyright income: 10,000 PLN;
- personal dependent services – income: 30,000 PLN;
- business activities – loss: 10,000 PLN.

Thus, Rob's total income amounted to 40,000 PLN. He will pay the tax on that income.

He did not obtain income from business activities, and he will be able to deduct the loss from income derived from that source over the next 5 years, provided that no more than 50% of the entire loss is deducted in a single year.

If we wanted to calculate Rob's total income as the difference between total revenue and total expenditure, we would have:

revenue: 81,500 PLN – expenditure: 51,500 PLN = 30,000 PLN.

If we determined the total income in the above manner, the loss from business activities (i.e. 10,000 PLN) would be covered with income from other sources. Unfortunately, pursuant to the Personal Income Tax Act, income must not be determined in this way.

Among the revenue sources listed in the Act there are also some sources that we treat "separately". In other words, we do not add them up to other income but we calculate the tax on such sources "on an individual basis".

Such sources include:

a) a business activity subject to the flat-rate tax;
b) income from securities (shares, bonds);
c) income that is settled according to the lump-sum scheme (such as prizes from competitions, or civil law agreements up to 200 PLN).

What is revenue?

According to the Personal Income Tax Act (PIT Act), "Revenue consists of money and monetary assets received by or made available to the taxable person during a calendar year, as well as the value of benefits received in kind and other free performances".

If you look the quoted article up in the Act, you will find that it contains reservations and indicates the sources of revenue to which this definition does not apply. Exceptions refer to revenue from the following sources:

1) non-agricultural business activities – here the revenue consists of amounts due, even if they have not been received;
2) special branches of agricultural production – here the income (and not the revenue) is estimated based on the size of agricultural production;
3) some capital gains – here the revenue can comprise amounts due or the value of shares that have been taken hold of;
4) sales of real property, cooperative ownership right to premises and other property (e.g. a car) – the revenue is the amount received less the selling costs;
5) not covered by disclosed sources, or coming from non-disclosed sources.

– here the amount of revenue is estimated based on a taxable person's expenditure.

We will deal with the exceptions in due time. Now let us have a look at the basic definition, in which several surprises are hiding too.

The first thing that should be noted is: revenue is not just money. In general, we can say that revenue also comprises non-financial benefits received by a taxable person. Such benefits may include, for example, a material bonus granted by the employer (e.g. a laptop for good work performance).

When it comes to money or monetary assets (with monetary assets including bills, bills of exchange, cheques, etc.), they become revenue if received by or made available to a taxable person. Basically, a person receives money when they get it into their hand but nowadays, money is usually made available to them. The moment that money becomes available is the time when a taxable person is able to use it.

Example:

Sean works in a factory. On the twentieth day of each month, the employees can pick up their monthly wages in cash at a corporate cashier's window. So usually there is quite a queue in front of the window on the twentieth of each month. Sean collected his last wages from the cashier's window as late as on 22 January. So when did revenue originate for Sean?

Although Sean received his wages on 22 January, it had already been made available to him on 20 January (because on that day he could go to the cashier's window and collect the wages).

Thus, the revenue day in this case will be the day when the wages was made available to the employee.

If revenue is made available to a taxable person, it means that the money or monetary assets are freely accessible for or can be freely used by the person. This will typically be the day when a relevant amount is credited to the taxable person's bank account or the day of payroll approval, which allows the person to collect their remuneration at the corporate cashier's window.

Currently, most of the revenue is transferred to taxable persons' bank accounts, which makes it problematic in practice to determine the moment when the revenue originated for a taxable person. Usually, some time elapses between a taxpayer's (e.g. an employer's) transfer order and the moment when the money is credited to a taxable person's account.

If we considered that revenue arose when money was made available to a taxable person (the person became able to freely use the money), we would say that revenue originates only when the money becomes "physically" credited to the taxable person's account. Unfortunately, a revenue paying entity (which is frequently required to collect a tax advance from such payment) is often simply unable to determine when the money will be credited to the receiving party's account.

Therefore, in real life, taxpayers assume that the revenue day is the day when they have debited their own bank account. Generally, tax authorities (for practical reasons) agree with this approach. If, however, some disputes arose concerning the issue, we should in fact consider that in the period between debiting the paying entity's account and crediting the taxable person's account, the money remains at the bank's disposal.

Although the concept of "making the money or monetary assets available" may raise some questions of interpretation, it is usually much more problematic to establish the meaning of the concept "money value of benefits in kind".

First of all, in the case of such revenue, we deal with a non-pecuniary performance. If an in-kind benefit or free-of-charge performance constitutes revenue, then – for tax purposes – we have to determine the value of such performance in cash.

Money value of benefits in kind is established based on market prices charged in trading in property or rights of the same kind and type, taking particularly into account their condition and wear, and the time and location when and where they are obtained.

Example:

Kate works in a supermarket. From time to time her employer gives the employees a bonus of foodstuffs and cosmetics. Of course, such a bonus is employee revenue. Its value should be determined based on market prices. In our example, it is most probable that the employer that manages the store gives the employees products from the store's range. So in this case, the market price will be the "shelf price", that is the one for which other customers of the store can buy the same products.

For free-of-charge performances (i.e. when a service or some other benefit is obtained), revenue is determined as follows:

- if a performance is related to services falling within the scope of a performing entity's business activity – the value is established based on the prices charged to other customers, i.e. in the same way as in the example above;

Example:

Employees of an outpatient dental clinic receive a performance consisting of free dental treatment and procedures.

In their case, revenue is determined at the equivalent of the price charged to other patients for the same treatments/procedures.

- if a performance is related to services purchased – the value is established based on purchase prices;

Example:

Christopher's employer rents an apartment for him. Christopher's revenue equals the amount paid by the employer for renting the apartment.

- if a performance consists of the provision of premises or a building – the value will be an equivalent of the rent that would be payable if a rental agreement was concluded for the premises or the building;

Example:

We have a situation similar to the above, but this time the employer does not pay the rent for the apartment where the employee stays, but provides them for free with, say, a company apartment. Here the revenue will be the "rental value". In other words, it must be determined what the price would be for renting a similar flat in a given locality, and the corresponding revenue should be determined at that amount.

- in other cases the value is established based on market prices charged on the provision of services or property or rights of the same kind and type, taking particularly into account their condition and wear, and the time and location when and where they are made available.

Example:

The company gives a company car to a member of the management board, which they use to go on 10-day holiday.

Obviously, it is the free use of the car that is the revenue here. Revenue should be measured at market prices; we should therefore determine how much we will pay for the rental of the same car type as the one provided to the board member for 10 days in a given locality.

For partially paid performances, a taxable person's revenue is the difference between the value of such performances, as determined in accordance with the above-mentioned principles, and the fee paid by the taxable person.

Example:

The employer partially finances Sally's trip abroad. The cost of the trip is 3000 PLN. Sally pays 1000 PLN, and the reminder of the sum is paid by the employer.

So Sally's revenue is 2000 PLN.

Revenue in foreign currencies is converted into PLN according to the average FX rate announced by the National Bank of Poland, as applicable on the last working day preceding the revenue day.

Example:

Ann completes a translation assignment for an Italian customer. She receives remuneration in EUR on 28 January 2013.

For tax purposes, the revenue should be converted according to the average exchange rate of the NBP, as applicable on the last working day preceding the revenue day. Since 28 January is Monday, the last working day preceding the revenue day will be Friday, 25 January.

Sources of revenue

Tax authorities are determined to tax as many sources of revenue as possible. Therefore, in principle, almost any revenue item is subject to the tax. Of course, there are exceptions to this rule: some revenue items are not subject to income tax, because they are excluded by a specific provision, and certain revenue items are tax-exempt.

Taxable sources of revenue (in accordance with Article 10 of the Personal Income Tax Act) include the following:

1) service relationship, employment relationship, including cooperative working relationship, membership in an agricultural production cooperative or other cooperative engaged in agricultural production, putting-out system, retirement pension or disability pension;
2) contractual professional services;
3) non-agricultural business activity;
4) special branches of agricultural production;
5) rental, subletting, lease, sublease and other contracts of a similar nature, including lease and sublease of special branches of agricultural production and an agricultural holding or its components for non-agricultural purposes or for management of special branches of agricultural production, with the exception of assets related to a business activity;
6) capital gains and property rights, including transfer of property rights for consideration;
7) transfer for consideration of:
    a. real property or parts thereof, and interest in real property;
    b. cooperative ownership right to residential or commercial premises, and the right to a single-family house in a housing cooperative;

c. the right of perpetual usufruct of land;
d. other property;
- if the transfer for consideration is not effected as part of a business activity and was completed: in the case of the sale of real property and property rights referred to in item a-c – before the expiry of 5 years following the end of the calendar year in which the acquisition or construction took place; and in the case of other property – before the expiry of six months following the end of the month in which the acquisition took place; in the event of an exchange transaction, such periods apply to each party to the transaction;

8) other sources.

Revenue from employment relationship (and related relationships)

This is certainly the most common source of revenue, because almost everyone was, is or will be an employee. In general, we can say that revenue from an employment relationship comprises all benefits received by an employee in connection with work. Importantly, they do not have to be benefits received directly from the employer.

Example:

Employees of a Polish company erect a building for a foreign counterparty of their employer. The foreign counterparty provides employees with a free accommodation. Although this benefit is not provided directly by the employer, it will be considered revenue from the employment relationship for tax purposes.

In accordance with Article 12 para. 1 of the Personal Income Tax Act, revenue from a service relationship, employment relationship, cooperative employment relationship or putting-out system is understood as all pecuniary payments and the money value of benefits in kind or their equivalents, regardless of the source of funding for such payments and benefits, and in particular:

- basic pay;
- overtime pay;
- various types of allowances;
- awards;
- payments in lieu of leave not taken;
- all other payments, regardless of whether their amount has been fixed in advance;
- pecuniary performances for the employee's account;
- value of other free or partially paid performances.

Pursuant to this provision, revenue from work is not limited to remunerations specified in the labour law regulations. Revenue also includes pecuniary performances, as well as the value of non-pecuniary performances, including free performances, regardless of their source of funding, and whether their amount was fixed in advance (e.g. in a contract of employment) or not.

The catalogue of revenue items given in Article 12 para. is not exhaustive. Therefore, revenue from employment relationship includes all performances/benefits received by an employee from their employer (or another entity) in connection with the current employment relationship or related relationship.

Employee

We should remember that revenue from an employment relationship may only be received by an employee. Thus, if a person receiving revenue is not an employee, they cannot obtain revenue from an employment relationship.

Within the meaning of the Personal Income Tax Act, the "employee" is a person remaining in the service relationship, employment relationship or cooperative employment relationship, or covered by the putting-out system.

This definition is much broader than that resulting from labour law (Labour Code), since the tax legislation understands the employee not only as a person remaining in the employment relationship and cooperative employment relationship, but also as a person remaining in the service relationship, or covered by the putting-out system. Therefore, the employee definition will not cover people who perform work under a contract of mandate, a specific-task contract, an agency contract or a management contract.

In-kind benefits or free-of-charge performances

Employees usually earn their revenue in cash, but not infrequently they receive in-kind benefits or free-of-charge performances. In order to determine the monetary value of such benefits and performances, we apply the general principles that we have already mentioned before.

Unfortunately, the activities of tax authorities and administrative courts are such that almost any performance/benefit other than a pecuniary performance for the employee becomes controversial and risky. Recent rulings of the Supreme Administrative Court (NSA) concerning medical packages, team-building events and commuting workers have proved unfavourable for both employees and employers, and they actually deepen the employers' uncertainty as regards the appropriate settlement of non-material and in-kind performances/benefits.

A survey conducted by one of the research institutes has shown that more than half of the companies have problems determining which non-pecuniary benefits have to be taxed, and which not. Many employers admit that they have resigned from granting employees benefits such as medical packages, company cars or company mobile phones precisely because of tax concerns.

In the case of non-pecuniary benefits, controversies usually boil down to the question of "receiving" such a benefit.

We should note that according to a general, basic definition, revenue consists of money and monetary assets received by or made available to the taxable person, as well as the value of benefits received in kind and other free performances.

As regards a pecuniary benefit, it originates not only when received by but also when made available to the taxable person. In the case of non-pecuniary benefits, revenue consists only of benefits received. So it is not enough for such benefits to be made available to an employee.

Example:

An employer buys swimming pool vouchers for its employees, so each employee can go to the swimming pool once a week for free.

The fact that the employer sponsors the swimming pool admission means that employees earn revenue.

This benefit is made available to employees (everybody can go the swimming pool) but the employee earns revenue only if and when they go to the swimming pool (i.e. when they receive the benefit).

The distinction between receiving a non-pecuniary benefit and having it made available is the subject of increasingly absurd court judgments.

Controversies are also associated with team-building events. The Supreme Administrative Court (in its judgment of 17 January 2012, II FSK 2740/11) stated nothing more nor less than the following:

“A free-of charge performance received is already (...) an opportunity granted to an employee to take advantage of the services purchased by the employer”.

Thus, contrary to the legal provision (and common sense), the Supreme Administrative Court concluded that the employee's tax obligation arises from the mere fact they have received an invitation to such event, regardless of whether the employee even took part in it and to what extent benefited from the proposed activities.

Another important issue related to the taxation of non-pecuniary revenue of an employee is the determination of its value. In a situation where an employee receives an in-kind benefit or free-of-charge performance, and it is not possible to determine which part of its value falls to the employee concerned, we will not deal with revenue. Revenue is in fact the value expressed in money of in-kind benefits or free-of-charge performances received by a taxable person.

Example:

Let us return to the example in which a swimming pool admission was made available to employees. We have determined that any revenue will arise only when an employee receives such a benefit, that is, when they go to the swimming pool.

If the employer in no way forces its employees to use the swimming pool and it does not record which employees and how many times used the benefit in a given month, then, in practice, we have a situation where the employee who visited the swimming pool received some revenue (or, in other words, received a benefit from their employer), but objectively speaking, it is impossible to determine the value of such revenue.

Example:

An employer running a general merchandise store gives to employees products (such as cosmetics and detergents) that are past their sell-by date.

The provision of the Act requires that such products for employees be valuated according to the prices charged to other customers. The owner would not have sold the products past their sell-by date, so the value of such products is zero. Consequently, such performance will not be a revenue item.

Revenue from contractual professional services

The catalogue of revenue items related to contractual professional services is quite broad.

To put it simply, such revenue is the revenue that is not derived from employment relationship or business activities.

In Article 13 of the Personal Income Tax Act, we find an exhaustive catalogue of such revenue items. The most popular and the most common are:

- revenue from contractual professional services: artistic, literary, scientific, coaching, educational and journalistic, including from participation in competitions in the field of science, culture and art, and journalism, as well as revenue from sports, sports scholarships awarded on the basis of separate regulations, and revenue of umpires/judges/referees related to sports competitions;
- revenue earned by persons sitting on management boards, supervisory boards, committees or other decision-making bodies of legal persons;
- revenue from civil law agreements, such as contracts of mandate and specific-task contracts (excluding contracts concluded as part of a taxable person's business activities).
- management contracts.

In order to determine the revenue from contractual professional services, we apply general principles, i.e. revenue consists of money (and monetary assets) received by or made available to the taxable person, as well as the value of benefits received in kind and other free performances.

Special branches of agricultural production

In general, agricultural activities are subject to agricultural tax, and as such remain outside the framework of Personal (and Corporate) Income Tax Act. However, the legislator has taken into account that some types of agricultural production are not necessarily associated with owning an agricultural holding and paying agricultural tax. In practice, they are closer to a typical business activity.

The catalogue of types of such agricultural production is quite broad, and includes among others: cultivation of ornamentals and mushrooms, breeding poultry and fur animals, apiaries, and breeding purebred dogs and cats.

In general, agricultural production that takes place outside an agricultural holding is treated as a specific type of business activity. A taxable person earning revenue from such activities may settle it according to the general tax scheme for business activities, or use simplified rules for determining the activity-related income (legal regulations provide for the estimation of income based on a "unit of production" such as one animal or one square metre of crop).

Revenue from capital gains

One of the sources of revenue in personal income tax consists of capital gains and property rights (also including transfer of property rights for consideration).

The most popular revenue items of this type include:

- bank interest (on loans, accounts, savings deposits, etc.);
- interest (discount) on securities, e.g. interest on bonds;
- dividends.

Although they belong to a single source of revenue, individual categories of income from capital gains are taxed in a different way. Some (dividends, interest) are taxed according to the lump-sum scheme, while others according to general rules.

Revenue from property rights

Revenue from property rights includes, in particular, revenue from copyright, rights to inventions, rights to integrated circuit topographies, trademarks and ornamental designs, and the transfer of such rights for consideration.

Thus, revenue from property rights is both revenue from the use of such rights (like licensing), as well as revenue from their transfer for consideration (such as sales of copyright to a novel by an author to a publishing house).

Revenue from transfer of real or other property for consideration

Sale of real property, land or a cooperative ownership right to premises is subject to the tax if it takes place before the expiry of 5 years following the end of the calendar year in which the acquisition or construction took place, and in the case of other property – before the expiry of six months following the end of the month in which the acquisition took place.

Revenue from such sales is the value expressed as the contractual price less the costs of transfer for consideration. These costs may be the costs of property valuation, stamp duty and notarial fee paid in respect of the contract.

We can say that revenue from the sales of real property will be the price (net of selling costs), provided that it corresponds to the market value. A tax authority can in fact determine the revenue at the market value, if the contractual price is significantly divergent from that value, and no reasons for the difference were given.

Example:

A notarial deed concerning the sale of a 50 sqm flat in Warsaw specifies the selling price of 100,000 PLN. Since in the opinion of a tax authority the price indicated in the deed is significantly divergent from the market value, the parties to the transaction have been requested to change the value or indicate reasons for having stated the price that is significantly divergent from the market value.

In response, the buyer and seller have made a statement that they are brothers and agreed on the below-market price because of family ties.

Before a tax authority determines revenue from the sales transaction in the amount other than resulting from the contract, it requests the parties to the transaction (not just one party but both of them, that is the buyer and the seller alike) to change the value or give the reasons why the price had been understated.

Where the parties to the transaction fail to respond, change the value or give the reasons justifying the understated price, a tax authority or fiscal inspection authority will determine the value based on the opinion of one or more experts. If the value determined in this way differs by at least 33% from the value expressed as the price, the cost of the expert opinion will be borne by the transferring party.

Exchange of real property

The term "transfer for consideration" as it appears in legal regulations does not only comprise a contract of sale, but also any other contract providing for a transfer of title for consideration, including a contract of exchange.

A tax obligation arises on the real property exchange as it does in the contract of sale, if the exchange takes place prior to the expiry of 5 years following the end of the year in which the acquisition took place. This period applies to each party involved in the exchange.

For each party to the transfer of title contract, revenue from the transfer for consideration by way of exchange of real property or property rights will be the value of real property or right that is transferred by way of exchange.

Other property

Sales or exchange of other property results in the tax obligation similarly to transactions concerning real estate. Tax revenue arises if sales of a property item takes place before the expiry of six months following the end of the month in which the acquisition took place.

Example:

Joan is summoned by the head of a tax office to account for revenue from the sale of an antique chair that she has sold via an Internet auction site. During the checks, Joan explains that the chair was a family heritage, which she has had in her apartment for many years, and as such the sales transaction does not result in a tax obligation.

Unfortunately, the tax official points out to her that in the item description on the website she wrote:

"A beautiful Boulle-style chair bought two months ago from a well-known collector from Cracow".

The tax authorities are becoming increasingly effective in enforcing taxes on Internet sales. We should remember that an auction description may attract not only the attention of potential buyers, but also of a tax official.

Other sources

The last source of revenue that we would like to discuss is "other sources". Generally, this category comprises all items that have not been included in the other categories. This catalogue is not exhaustive, due to the fact that tax regulations often lag behind real life, and even the tax legislator is unable to predict all potential sources of revenue.

Legislation only provides examples of revenue items that do not fall into this category:

- amounts paid following the death of an open pension fund member to a person designated by the deceased or to a member of their immediate family;
- cash benefits from social insurance (sickness allowance, family allowance, carer allowance, etc.);
- maintenance (alimony), scholarships, grants (subsidies);
- revenue not covered by disclosed sources.

Particular attention should be paid to revenue not covered by disclosed sources, or coming from non-disclosed sources. Such revenue is very interesting for tax authorities. Seeking for and taxing such items is among the main priorities of the Polish tax authorities.

This revenue is, generally speaking, that revenue which a taxable person wanted to hide from the tax authorities.

How does a tax authority find about such items? Suspicions that a taxable person has failed to reveal their entire revenue in, say, their annual tax returns may arise if they spend more than they "officially" earned.

Most frequently, tax authorities learn about a taxable person's spending from notarial deeds that civil law notaries must file with the official authorities. So a taxable person who, for example, has bought some expensive real property and at the same time disclosed a modest income in their annual returns will obviously find themselves in the tax authorities' sights. After all, the money to buy the real property must have come from somewhere. And if the revenue disclosed in the annual returns is insufficient to make such a purchase, the difference probably comes from "undisclosed income".

Example:

Christopher is a young man, just out of college. So far he has not filed any tax returns because he never worked in Poland. However, he has recently bought a flat. This attracted the attention of a tax authority which initiated checks to verify what sources were used to finance the purchase and why no such sources had been disclosed for tax purposes.

Christopher explains that the flat has been purchased with cash, and the source of cash is: multi-annual family savings, which he received from his uncles, grandparents, and other family members, and from the withdrawal of funds from his mother's building society book opened in 1978. All this time, Christopher was supported by his family and did not work in Poland. He went to the United States twice (as part of Work & Travel programme), where he earned some money from waiting tips.

The proceedings concerning undisclosed revenue are usually long and very complicated.

In our example, the tax authority would carefully scrutinize the sources that the taxable person invokes, and it would establish whether the persons that Christopher named have actually made cash gifts to him, and if so, whether such gifts were taxable and finally, whether the amount raised would be enough to purchase the real property.

If it turns out that the amount of revenue from sources "disclosed" in this way is still insufficient, or if the tax authority does not find the taxable person's explanations credible, then the authority would be authorised to apply the penalty tax rate of 75%.

We have not mentioned here one of the most important sources of revenue, that is non-agricultural business activities. Indeed, we devote a separate section to the topic.

Personal Income Tax. Revenue expenditure: General rules

Revenue expenditure consists of expenses that reduce revenue, thus resulting in income, i.e. the taxable base. Therefore, the amount of tax we pay largely depends on revenue expenditure.

Example:

Simon and Josh share the same workplace, where they earn a basic salary of 2000 PLN. Simon lives in the town where the company establishment is located. That is why he is entitled to basic revenue expenditure of 111.25 PLN. Josh lives in another town, so he commutes to work. Therefore, he is entitled to higher revenue expenditure, namely 139.06 PLN/month.

As a result, Simon and Josh pay a monthly advance tax amounting to 111 PLN and 106 PLN respectively. With different revenue expenditures, Josh will pay tax reduced by 5 PLN, even if he earns the same revenue.

Although Josh gets 5 PLN more in salary, it is obvious that this amount does not compensate him for commuting expenses.

Definition of revenue expenditure

Both Income Tax Acts contain the same definition of revenue expenditure:

Revenue expenditure is expenditure incurred to generate revenue or to maintain or secure a source of revenue, except for expenditure listed in the Act as not included in the scope of revenue expenditure.

So the definition is short and rather simple. We write "rather" because the definition features a logical error: both the defined and defining part contain the word "expenditure", that is: "revenue expenditure is expenditure". Let us assume, however, that such wording was used by the legislator to say that tax expenditure (i.e. revenue expenditure) is the expenditure in both linguistic and economic terms.

In order for expenditure in a general sense to be considered tax expenditure it must be incurred for a specific purpose (to generate revenue or to maintain or secure its source).

The definition is very general. It would be difficult, however, to give a more precise definition: it would be equally true if we say that on the whole, expenditure can be anything, provided that it relates to obtaining revenue.

Based on the above-mentioned definition, it is possible to determine the necessary conditions for an expense (i.e. the expenditure in a linguistic sense) to be considered a tax expenditure item:

1) The expense must be actually incurred.

Therefore, no events resulting solely from accounting transactions, such as inventory revaluation can be considered expenditure. If any expense is incurred, it must be documented or otherwise proved.

2) The expense must be incurred to generate revenue or to maintain or secure a source of revenue.

The expense must be related to revenue. This relationship, however, as we will discuss soon, may be direct or indirect. In any case, this relationship should be unquestionable.

Example:

An entrepreneur has concluded an unfavourable contract to sell their services. Unfortunately, a contractual indemnity applies for termination. The analysis shows that performance of the contract will bring about greater losses than its early termination and payment of the indemnity. Could the payment of contractual indemnity in this situation be considered revenue expenditure?

This is only one example showing that classification or non-classification of an expense to tax expenditure is not simple at all. In the example above, there are some arguments for recognition of the expense under revenue expenditure: a taxable person decides to terminate the contract and pays the applicable indemnity to protect their sources of revenue (in order to limit losses).

The tax authorities may, however, see the situation in a different way: by paying the indemnity, the taxable person is not acting to generate revenue, or secure/maintain its source. Actually, the expense is incurred in order to eliminate a source of revenue,

3) The expense may not be included under “prohibited expenditure”.

Both Income Tax Acts include a catalogue of expenses that will not be considered revenue expenditure. Consequently, even if the expense was incurred to generate revenue, but is included in the “prohibited list”, it will not be revenue expenditure.

A separate section will be devoted to such expenses.

Direct and indirect expenditure

A relationship between revenue and expenditure may be direct or even very indirect.

Example:

A shop sells toothpaste for 7 PLN. It buys the product from a wholesale outlet for 4 PLN. In this case, the expense on purchasing the toothpaste, i.e. 4 PLN, is a direct revenue expenditure item. In order to obtain revenue from sales of the toothpaste (7 PLN), it was necessary, in the first place, to buy the product. If no expenditure had been incurred, there would be no revenue.

So in practical terms, direct expenditure consists of expenses that are indispensable to generate revenue.

With indirect expenditure, things are not so simple though. It cannot be linked directly to a specific revenue item, but there is no doubt it is necessary and justified.

Example:

A grocery shop employs a part-time cleaning lady whose salary is 900 PLN. The employee's salary will be an indirect expenditure item. This is because it is difficult to link the salary to specific revenue. Also, it cannot be unambiguously stated whether the cleaning lady's work translates into increased revenue of the shop. Theoretically, yes: few people would like to shop in a dirty place. In this case, the connection with revenue, though not direct, is rather obvious. The tax authority would have no doubt that such expense can be revenue expenditure.

Example:

John runs a business and provides repair services as part of it. In February, he books a climbing course and he would like to post that expense as revenue expenditure.

Certainly, John will have a problem explaining how the expense is related to the generation of revenue or securing its source. Indeed, it is not easy to indicate how climbing skills could come in handy for a person providing repair services.

This of course does not necessarily mean that the expense cannot be considered revenue expenditure. It is possible that John is planning to expand his business with other services such as skyscraper window cleaning, in which case this expense will no longer be doubtful. He can also perform repairs at height, so the acquisition of climbing skills becomes obviously related to revenue generation.

The above examples show that indirect costs are more problematic in interpretation, and therefore nearly all expenditure disputes between taxable persons and tax authorities concern indirect expenditure.

In order to be recognised under revenue expenditure, an expense must seek to generate revenue or maintain/secure a source of revenue. Maintenance and securing of a source of revenue means that expenses are incurred so that the "infrastructure" for earning money could serve its function further.

Example:

Trevor is engaged in a transport service business. He intends to suspend his activity for 4 months due to a lack of new assignments. Throughout the suspension period, he will continue to bear the expenses related to vehicle maintenance (restoration, fluid replacement, and overhaul). Could such expenses be considered revenue expenditure?

Yes. The expenses incurred are related to securing and maintenance of a source of revenue: it is clear that if Trevor wants to generate revenue after the suspension period, he must maintain his vehicle in a good state of repair.

Expenditure accounted for the cash or accrual basis

In essence, expenditure is deducted only in the year in which it has been incurred. This approach is known as the cash-basis recognition of expenditure.

Example:

An entrepreneur selling their goods online sold a product on 29 December 2012 and on the same day the customer's payment was credited to their bank account. The parcel was sent on 3 January 2013 and on the same day the entrepreneur paid the postage of 10 PLN. In the books, for which tax year will they post this expenditure?

Although shipping costs are related to the transaction from 2012, in accordance with the cash basis principle, they must be allocated to 2013 expenditure.

Tax regulations also provide for the accrual principle in expenditure classification.

The accrual basis for expenditure accounting is employed by corporate income tax payers and by self-employed persons who carry out full bookkeeping. The accrual basis for expenditure may also be used by taxable persons that keep the tax book of revenue and expenditure, provided that they choose this way of accounting, and that their records allow for a proper classification of expenditure.

According to this principle, revenue expenditure that is directly related to revenue, incurred in the years preceding the tax year and in the tax year itself, is deductible in the tax year in which corresponding revenue was generated.

Example:

If the entrepreneur from the previous example accounted for their expenditure on the accrual basis, then:

1) revenue was generated in 2012, as they received payment in that year; although revenue arises at the date when goods are delivered (here on the shipping day), but not later than at the date of invoice or settlement of the amount due, since the amount due was paid in 2012, the revenue was generated in 2012 as well;
2) order shipping is the expenditure directly associated with the corresponding revenue: in order to generate revenue from sales of the product, the entrepreneur had to bear the cost of shipping.

So in the accrual-basis settlement, the shipping cost should be considered the expenditure of 2012.

However, one significant point should be raised here. Revenue expenditure that is directly related to revenue, relating to revenue of a given tax year but incurred after the end of that tax year by the date of:

- preparation of financial statements, in accordance with separate regulations, but not later than the expiry of the deadline set for the submission of the statements, if a taxable person is obliged to prepare such statements; or - submission of tax return, but not later than the expiry of the deadline set for the submission of such return, if a taxable person, in accordance with separate regulations, is not obliged to prepare financial statements;

- is deductible in the tax year in which the corresponding revenue was generated.

If the entrepreneur (an individual) from our example submitted their annual tax return for 2012 on 2 January, he would have to include the shipping costs among 2013 expenditure, even if they accounted for expenditure on the accrual basis.

This rule is intended to avoid the need to correct annual returns if expenditure was incurred in a new tax year that would be directly related to the previous year's revenue.

Thus, if a taxable person has not yet closed the previous year (or the deadline to do so has not expired), then such expenditure must be recognised in the previous year. If the year has been already closed (by way of submission of an annual tax return or preparation of financial statements), then direct expenditure must be recognised under the current year's expenditure.

Important!

Expenditure can be settled on the accrual basis only if it is directly related to specific revenue.

Revenue expenditure other than expenditure directly related to revenue is deductible on the day when it is incurred.

If such expenditure is related to a period longer than a tax year, and it is not possible to determine what part of it refers to a particular tax year, then it is considered revenue expenditure in the part corresponding to the length of the period to which they refer.

Example:

In March the company buys an annual subscription to a professional monthly magazine for 500 PLN (subscription period: April-March).

As the expenditure is related to a period longer than a tax year, it has to be accounted for pro rata. Out of 12 issues of the magazine, 9 refer to the first year, and 3 to the following one.

So the expenditure of the first year will be the amount of 375 PLN, and of the second one will be 125 PLN.

Sometimes, however, there is no way to determine whether indirect expenditure applies to the period and what the period is.

Example:

Entering lease payment is commonly referred to as the lessee's own contribution.

For tax authorities, the character of this payment is not clear though. At times, they issue interpretations where they recognise that the entering payment is not dependent on the lease duration, and agree that it should be entirely recognised among expenditure on the day when it is incurred, and sometimes they are of opinion that the payment should be settled in proportion to the lease period.

Day of revenue expenditure

A day of revenue expenditure is understood as the date when the expenditure was recognised (posted) in the books of account on the basis of a received invoice (bill), or the date when it was recognised on the basis of other evidence, if no invoice (bill) is available.

Documenting expenditure

An important, yet very troublesome issue, is that of expenditure documentation. In accordance with legal regulations, any expenditure should be properly documented, such as with an invoice or other document (i.e. payroll).

Although legal provisions in both income tax acts do not mention the issue of documenting expenditure, precise rules are delimited in the regulations concerning tax records keeping.

Therefore a question arises: could an expense that clearly meets the definition of revenue expenditure but has not been properly documented be posted as this type of expenditure?

Example:

An inspection at the premises of a taxable person operating a bakery shows that the size of business is understated. On the basis of documented purchases of flour, it is noted that the quantity is enough to bake 100,000 loaves of bread, while other evidence shows that the sales amounted to at least 150,000 loaves. The taxable person argues that they have supplied documented purchases with other purchases from parties that did not issue for them any corresponding bill or invoice.

Consequently, the tax authority estimates the revenue based on the acknowledged sales, while the expenditure remains unchanged, since, according to the tax authority, the taxable person has failed to prove that they have incurred expenses higher than the documented amount.

Was the tax authority's approach correct?

Although more often than not the tax authorities' approach is like the one described in the example above, it should be considered to be incorrect. The tax authority has determined that the taxable person baked and sold 150,000 loaves of bread, whereas the accounting records only documented the purchase of flour for baking 100,000 loaves. In other words, the taxable person must have had flour to produce another 50,000 loaves. Most likely, flour was bought, but for some reason this fact is not documented. The fact that relevant expenditure was incurred may actually be proved with any credible evidence. "One cannot share the authorities' view that a taxable person that did incur expenditure but has no evidence to prove it, will not be entitled to recognise such expenses as revenue expenditure. It should be noted here that the provisions of the Act regarding revenue expenditure do not define the rules for documenting the fact that the expenditure was incurred" (judgment of the Supreme Administrative Court of 13 March 2001, III SA 68/2000, Przegląd Podatkowy 2001, Vol. 10).

In practice, the above rules governing classification and establishment of revenue expenditure apply to the source of revenue in the form of a non-agricultural business activity.

In the case of revenue from other sources, specific expenditure provisions associated with a particular source of revenue will apply.

Revenue expenditure in employment relationship

Unfortunately, employees can hardly influence the amount of their tax expenditure. If revenue is derived from an employment relationship, expenditure is determined at a lump-sum amount specified in legal regulations. As a result, employees cannot apply real expenditure to their settlements (such as expenditure on reading material or self-education).

The lump-sum staff expenditure:

a) amounts to 111.25 PLN/month, and not more than 1335 PLN per tax year – if a taxable person derives their revenue from one service relationship, employment relationship, cooperative employment relationship and putting-out system;

For a hired employee, the employer deducts monthly expenditure of 111.25 PLN, which in the case of a full year of employment gives the amount of 1335 PLN (12 x 111.25 PLN).

b) must not exceed the total of 2002.05 PLN per tax year – if a taxable person derives their revenue from more than one service relationship, employment relationship, cooperative employment relationship and putting-out system;

If an employee works several jobs, each employer deducts for them 111.25 PLN as revenue expenditure, which does not mean that the employee will be able to disclose the full amount of expenditure thus recognised by all employers in their annual tax return, as in this case the expenditure ceiling applies.

Example:

Ann is employed in two companies. Therefore, after the year end, she received a PIT-11 tax form from each employer, stating the revenue expenditure of 1335 PLN.

However, in her annual return, she will not disclose the sum total of such expenditure (i.e. 2670 PLN), because in the case of "multi-employer employees", the expenditure must not exceed 2002.05 PLN, so this is the amount that Ann will disclose in her tax return.

c) amounts to 139.06 /month, and not more in total than 1668.72 PLN per tax year, if a taxable person is permanently or temporarily residing in a locality other than where the company establishment is located, and the taxable person does not receive the expatriation allowance;

d) must not exceed the total of 2502.55 PLN per tax year – if a taxable person derives their revenue from more than one service relationship, employment relationship, co-operative employment relationship and putting-out system, and a taxable person is permanently or temporarily residing in a locality other than where the company establishment is located, and the taxable person does not receive the expatriation allowance.

An employee who commutes to work (because they live or stay in a locality other than where the company establishment is located) is entitled to increased tax expenditure. In order to be able to apply increased revenue expenditure, the employee must jointly satisfy three conditions:

1) the employee's place of permanent or temporary residence must be located outside of the locality where the company establishment is located; it should be emphasized here that the condition refers to the place of residence (or temporary stay), and not the permanent registered address; also it is the place of work that matters and not the registered address of the employer;

Example:

The place of residence of an employee is the same as the registered address of the enterprise that employs them, yet the establishment in which the employee actually works is located in a different locality than the enterprise's registered office.

In this situation, the employee will be entitled to apply expenditure at an increased rate.

2) does not receive the expatriation allowance;
3) is not reimbursed for the costs of commuting, except when the expenditure reimbursed has been recognised as taxable revenue.

If a taxpayer (employer) wants to apply increased revenue expenditure while calculating withholding tax, they must receive the employee's statement of compliance with the above-mentioned conditions (Article 32 para. 5 of the PIT Act). If an employee does not submit a relevant statement, the employer will not be able to charge higher expenditure while calculating withholding tax. However, this does not deprive the employee of the right to charge higher expenditure in their annual tax return.

A one-time statement is enough, as it remains valid in subsequent tax years, until a change to the facts is notified, such as change in place of residence.

When an employee ceases to satisfy the conditions for application of higher revenue expenditure, the employer calculates withholding tax with the use of a basic expenditure rate starting from the month following the month in which the employee ceased to satisfy the conditions for a reduction in tax advances.

If the annual lump-sum expenditure to which the employee is entitled is lower than their actual expenses in commuting to their place(s) of work by bus, train, ferry or public transport, then in the annual tax return such expenditure may be adopted at the amount of expenses actually incurred, but only when the employee will document such expenses with personal season tickets.

Example:

John commutes to work by train. Therefore, he buys a monthly ticket for 170 PLN.

Consequently, his annual commuting expenses reached 1870 PLN (11 months x 170 PLN; in July John did not buy a monthly ticket because he was on holiday).

We can see that his total commuting expenses are higher than the lump-sum expenditure. Therefore, in his annual tax return John will disclose the expenditure of 1870 PLN rather than 1668.72 PLN.

Lump-sum staff revenue expenditure is only applicable when the employee's revenue was only derived from the employment relationship. Such expenditure may be used by part-time employees and those on annual leave.

However, the amount of expenditure that may be included in the annual tax return will depend on the number of months worked in the tax year.

Example:

If an employee is employed under an employment contract in January, February and March, and in November and December 2012, then in the settlement for the year 2012, they will take into account tax expenditure only for those 5 months.

Importantly, an employee who has entered with one (and the same) company into one or more contracts of employment, is connected to the company with several employment relationships, and thus separately entitled to: annual leaves under each employment relationship, a certificate of work, and specific benefits (if any) such as long service pays, retirement gratuities, etc., which means that the conclusion of each contract is treated as a separate employment relationship and on an equal footing with contracts concluded with various employers.

Consequently, in order to establish staff revenue expenditure, it should be assumed that any separate contract of employment entitles the employee to revenue expenditure, regardless of whether they have been concluded with one or more employers.

Lump-sum revenue expenditure from other sources

Lump-sum revenue expenditure applies not only to revenue derived from an employment relationship. In the case of revenue derived from civil law agreements in general, lump-sum expenditure amounts to 20%-50% of revenue (with the expenditure calculated on the revenue net of social security contributions).

Lump-sum revenue expenditure: 20%

This can be applied by taxable persons who derive their revenue within the framework of contractual professional services, i.e. under contracts of mandate, specific-task contracts, or as part of a liberal profession.

Example:

Determination of the expenditure amount in the case of a contract of mandate, when a contractor is subject to compulsory social insurance:

Revenue: 2000 PLN;

Social security (ZUS) contribution financed by the contractor: 13.71% (9.76% pension insurance + 1.50% disability insurance + 2.45% sickness insurance):

2000 PLN x 13.71% = 274.20 PLN;

Revenue expenditure: 20%:

1725.80 PLN x 20% = 345.16 PLN;

(revenue 2000 PLN – social security (ZUS) contribution 274.20 PLN = 1725.80 PLN).

If a taxable person can prove that their actual expenditure is higher than the lump-sum standard rate of 20%, then they have the right to apply the actual expenditure. Such expenditure should be documented with proof stating that it has been incurred (usually an invoice).

Lump-sum revenue expenditure: 50%

A form of tax preference is 50% expenditure to which authors are entitled in general. Such expenditure applies to revenue:

- against payment to the author for the transfer of title to an invention, integrated circuit topography, utility model, industrial design, trademark or ornamental design;
- against payment of a licence fee for the transfer of the right to use an invention, integrated circuit topography, utility model, industrial design, trademark or ornamental design, received in the first licence year from the first entity with which a licence agreement has been concluded;
- against the exercise of copyright by authors and of derived rights by performing artists, as defined by separate regulations, or effecting dispositions of such rights.

Of course, the most numerous group entitled to such expenditure are authors who derive their revenue from the exercise of copyright. It is a tax preference resulting from the fact that in the case of authors, it is difficult to indicate their actual expenditure. On the other hand, the legislator suggests by this preference that it promotes creativity and the artistic output of its citizens.

With a 50% expenditure rate, the tax is in fact paid on half of the revenue.

Importantly, 50% revenue expenditure can be applied not only by persons co-operating on the basis of a civil law agreement, but also by persons employed provided that they effect dispositions of copyright as part of employment relationship (e.g. by transferring it to the employer). However, a contract of employment should specify which part of the employee remuneration refers to the author's fee related to the employee's exercise of copyright, and which part is related specifically to the performance of the employee's (business) duties.

Pursuant to the Copyright Act, the object of copyright is any manifestation of creative activity of individual character, established in any form, regardless of the value, purpose and manner of expression (work). It must therefore be an original and manifested intellectual creation. For a product of human intellect to be considered a work, it must jointly display three characteristics:

a) it must be the result of human labour (the author's effort);
b) it must be a manifestation of creative activity (the work must be original and distinctive);
c) it must have an individual character (has such work been already created? would it be possible for someone else to create it?).

If the work contains an element of individual creative activity, then we deal with a work and an author.

Legal regulations specify possible objects of copyright (e.g. musical, artistic and photographic works), and things which could not be considered works (e.g. official documents or simple press releases).

Higher expenditure related to the transfer of copyright can be applied by employees and persons performing specific task contracts (or contracts of mandate). Such expenditure does not apply to works created in the course of business activity.

Employers are often unaware that if their employee "creates works" as part of their job, they are entitled to 50% of revenue expenditure. Tangible benefits may be obtained if such revenue expenditure is applied.

Example:

Peter Jackson owns a small advertising agency in Warsaw.

He employs 5 people under contracts of employment. Each employee earns 5000 PLN gross/month. Employees demand a pay rise, which the owner simply cannot afford.

At the moment, the employees' net pay is calculated as follows:

Gross remuneration: 5000 PLN;

Social insurance (ZUS) contributions: 5000 PLN x 13.71% = 685.50 PLN;

Basis for calculation of the health insurance contribution: 4314.50 PLN x 9% = 388.31 PLN (deduction amount: 334.37 PLN);

Income tax advance: 5000 PLN – 111.25 PLN (staff revenue expenditure) – 685.50 PLN (ZUS) = 4203.25 PLN;

4203 PLN x 18% – 46.33 PLN (1/12 of the tax credit) = 710.21 PLN.

The advance is reduced by a deductible health insurance contribution:

710.21 PLN – 334.37 PLN = 376 PLN (in rounded PLN).

So, the employee's 'clear' (net) remuneration is:

5000 PLN – 685.50 PLN – 376 PLN – 388.31 PLN = 3550.19 PLN.

Undoubtedly, the advertising agency employees are authors vested with copyright. Consequently, they are authorised to 50% revenue expenditure (the contract of employment should specify what part of the remuneration refers to the transfer of copyright to the employer, and what part is related to "ordinary" job-related duties). It might be assumed that 90% of the employee remuneration, i.e. 4500 PLN, refer to copyright, and 500 PLN is earned for other job-related duties.

Consequently, to the amount of 4500 PLN we could apply the 50% rate of revenue expenditure, and to the remaining 500 PLN, lump-sum staff revenue expenditure (111.25 PLN). Now, the employee's net pay may be calculated as follows:

4500 PLN x 13.71% (ZUS) = 616.95 PLN;

Revenue expenditure: (4500 PLN – 616.95 PLN) x 50% = 1941.53 PLN.

Income tax advance:

5000 PLN – 2052.78 PLN (revenue expenditure, i.e. 1941.53 PLN + 111.25 PLN) – 685.50 PLN

(ZUS) = 2261.72 PLN;

2262 PLN x 18% – 46.33 PLN = 360.83 PLN.

The advance is reduced by a deductible health insurance contribution:

360.83 PLN – 334.37 PLN = 26 PLN (in rounded PLN).

So, the employee's 'clear' (net) remuneration is now:

5000 PLN – 685.50 PLN – 26 PLN – 388.31 PLN = 3900.19 PLN.

So using the discretionary opportunities given by the PIT Act, the employee's remuneration has increased by 350 PLN.

Amendments effective since 2013

In looking for additional savings and proceeds, tax authorities have decided to reach into the pocket of authors.

Starting from 2013, a ceiling will apply to 50% revenue expenditure, namely the total revenue expenditure at that rate cannot exceed 1/2 of the upper limit of the first taxable band referred to in Article 27 para. 1.

In other words, the amount of revenue expenditure at the rate of 50% under titles referred to above cannot exceed 42,764 PLN. Consequently, the losers will be those authors whose relevant annual revenue is higher than 85,528 PLN.

Example:

Comparison of an author's tax burden in 2012 and 2013

A popular author wrote a book. He sold his copyright to a publishing house for 100,000 PLN.

In 2012 to that revenue we would have applied 50% revenue expenditure in full (50,000 PLN). As a result, the publishing house would have deducted the tax advance of 18% on the following income: 50,000 PLN x 18% = 9000 PLN.

In 2013, a maximum amount of authors' revenue expenditure must not exceed 42,764 PLN. As a result, our writer will earn an income of 57,236 PLN, on which the publishing house will deduct a tax advance of: 57,236 PLN x 18% = 10,302 PLN. In other words, the deduction will be by 1302 PLN higher than in 2012.

Revenue expenditure applicable to revenue from transfer of real or other property for consideration

As we know, revenue from sales of real and other property is taxable (if the transfer of real or other property occurs within 5 years or 6 months after the acquisition respectively). Here the taxable component is income, i.e. the difference between revenue and expenditure.

Revenue expenditure in the transfer of real or other property for consideration consists of documented costs of acquisition or manufacture gross of any documented outlays that have increased the value of such property and property rights as made in the period when they have been held.

Example:

In 2009 Joan buys a flat for 300,000 PLN. She fully renovates the flat (window, floor and system replacement), which costs her a total of 60,000 PLN.

In 2012 Joan sells the flat for 500,000 PLN. What revenue expenditure applies here?

In the first place, the expenditure consists of the cost of acquisition, i.e. 300,000 PLN. Another expenditure item consists of outlays that have increased the real property value in the period when Joan held it. It is obvious that a full renovation adds up to the property value, so the total expenditure is 360,000 PLN, and the resulting income is 140,000 PLN.

If the real or other property is acquired free of charge (for instance by inheritance or donation), we obviously do not have to do with any cost of acquisition or manufacture. So revenue expenditure in the case of acquisition free of charge consists of documented outlays that have increased the value of property and property rights when they were held, and the amount of inheritance and donations tax paid in that part in which the value of the property or right being transferred taxable with inheritance and donations tax corresponds to the total value of property and property rights taxable with inheritance and donations tax.

Summary

Income of a taxable person is influenced by both the revenue earned and the expenditure incurred.

Consequently, revenue expenditure is vital for tax burdens.

No wonder that all taxable persons strive for recognition of their expenses as revenue expenditure to the widest possible extent.

It is the self-employed who are able to shape their expenditure and thus their taxes to the largest extent, because they can establish their actual expenditure.

Taxable persons who derive their revenue from other sources (employment, revenue earned within the framework of contractual professional services) are definitely less free in this respect, as they are usually forced to apply the statutory lump-sum revenue expenditure.

PERSONAL INCOME TAX. REVENUE AND EXPENDITURE OF A SELF-EMPLOYED PERSON

Tax regulations offer to entrepreneurs a choice of several forms of business taxation. Therefore, let us determine first what conditions must be fulfilled in order to use each option, and attempt to decide how to select the most advantageous one.

Contrary to appearances, determination on the basis of tax regulations whether a taxable person derives their revenue from a business activity, or perhaps from another source, is not simple. Indeed, the tax authorities' position on this issue is often different from the taxable person's view.

Choice of a legal form for the entrepreneur

An entrepreneur who undertakes a business activity expects to achieve various objectives. The subject matter and scope of business influence its form. Polish regulations allow business to be conducted in a variety of forms:

a) self-employment;
b) civil partnership;
c) general partnership;
d) limited partnership;
e) limited partnership based on shares;
f) limited liability partnership;
g) limited liability company;
h) joint stock company;
i) branch;
j) agency.

In tax terms, the form of business activity listed above may be subject to personal income tax or corporate income tax.

Income tax forms

While deciding which form of business to choose from the list above, one should also consider the tax-related obligations. It may be that the choice of organisational form will be justified by tax savings.

Legal persons and other organisational units that do not have the status of individuals are subject to corporate income tax. Entities that are subject to corporate income tax have no choice when it comes to the tax form or rate.

The basic tax rate is 19% on the taxable base.

Individuals can pay income tax according to one of the following schemes:

- according to taxable bands – depending on income, a taxable person is subject to the rate of 18% and 32% (general scheme);
- at the uniform rate of 19% – regardless of income (flat-rate scheme);
- as a lump-sum amount on registered revenue;
- as a fixed amount ("tax card").

Taxable bands

Taxable bands are the basic taxation scheme, available to all entrepreneurs, regardless of the type of business. In this scheme, the tax is paid on income, i.e. the difference between revenue and expenditure. The tax is progressive, which means that the tax rate rises with income.

With this taxation scheme, an entrepreneur can use all available tax reliefs (e.g. family relief, Internet relief, or rehabilitation relief).

This method can be recommended to entrepreneurs whose income falls within the first taxable band (i.e. is not higher than 85,528 PLN), who are entitled to tax reliefs, or who would like to settle their tax on preferential terms jointly with a spouse, or who are single parents.

In this taxation scheme, an entrepreneur is obliged to keep a tax book of revenue and expenditure, in which they record both revenue and expenditure items. If the enterprise's revenue exceeds 1,200,000 EUR, the entrepreneur is obliged to keep books of account in accordance with the Accounting Act.

Flat-rate tax

Like taxable bands, this scheme is also available to all types and sizes of business. The only restriction applies to persons who provide services to their former employers. A taxable person loses the right to choose this taxation scheme if, as part of their business activity, they will render services for their former or current employer, corresponding to the activities that they have performed or perform as an employee in the same tax year.

Example:

Until the end of May, Ryan had been employed at Leaps&Bounds as a driver. In June he starts his own business for which he chooses the flat-rate tax scheme. In September his former employer orders from Ryan a training course for its employees. If Ryan renders the service, will he lose the right to the flat-rate tax scheme?

No. Although Ryan will render a service for his former employer in the same tax year, it will be a different service from the activities that he performed formerly in the context of employment.

The main advantage of this form of tax settlement is the low tax rate of 19% that is applied to all income from business activity, regardless of its amount. Unfortunately, with this taxation scheme it is not possible to take advantage of most tax reliefs and preferences.

In addition, the tax is paid on all earnings (no tax-free allowance applies).

This taxation scheme can be recommended to persons who earn high incomes and are not entitled to tax reliefs (or if they are, the use of such reliefs will be less favourable for them than the general scheme).

In this taxation scheme, an entrepreneur is also obliged to keep a tax book of revenue and expenditure, or books of account if their revenue exceeds 1,200,000 EUR.

Lump-sum amount on registered revenue

This taxation scheme can be opted for by the self-employed, or by partners in a civil partnership or general partnership. Here the revenue amount is the limit. The lump-sum scheme cannot be used by entrepreneurs whose revenue exceeds 150,000 EUR. If the threshold is exceeded, an entrepreneur loses the right to use the lump-sum scheme in the following year, and must settle their taxes under the general scheme (based on taxable bands).

Another limitation is that many types of business activity have been excluded from the lump-sum taxation scheme (examples include pharmacies, pawn shops, bureaux de change, and some liberal professions, such as tax advisors and architects).

The advantage of the lump-sum scheme is that an entrepreneur does not have to keep a book of revenue and expenditure (or books of account), as is the case in the general and flat-rate tax scheme. The entrepreneur only keeps a simplified record of revenue. This is because of the fact that the operating expenditure is not included in tax settlements. The tax is paid on revenue and not on income, but generally at lower rates. These are: 20%, 17%, 8.5%, 5.5% and 3% – depending on the type of activity.

There is no possibility to submit tax returns with a spouse, or according to the conditions laid down for single-parent families. Other tax reliefs are also available.

Fixed-amount tax ("tax card")

This scheme of taxation can be used by persons engaged in petty trading, catering and other service activities, either individually or in a civil partnership, as well as in some liberal professions.

This is the simplest of taxation schemes. One does not have to calculate business revenue or expenditure: the tax is paid monthly at a fixed amount specified in the tax office's decision. The tax is only reduced by a health insurance contribution. No other reliefs or deductions apply. It is also not possible to use a preferential tax treatment for marriages or lone parents.

The advantage of the “tax card” scheme is that no record keeping is required for tax purposes. However, the amount of tax specified in the tax office's decision may at times be higher than the tax in other taxation schemes.

Taxation scheme: selection criteria

While choosing one of the taxation schemes available for businesses, taxable persons are frequently guided by the anticipated amount of tax to pay. However, other criteria should also be considered here, such as:

a) costs of record keeping and settlements;
b) tax risk;
c) ability to influence the tax burden.

It should be considered that the lower tax-related expenditure (total costs of record keeping and settlements, and above all, the amount of tax to pay), the smaller the tax risk and the greater the taxable person's impact on the tax burden – the more favourable the taxation scheme.

Costs of record keeping and settlements

The simplest criterion for selection of taxation scheme consists of the determination of costs related to tax record keeping and tax settlements. Therefore, the hierarchy of the most convenient taxation schemes is as follows: fixed-amount tax (“tax card”), lump-sum tax on registered revenue, general flat-rate tax, and progressive tax calculated based on the tax book of revenue and expenditure.

In terms of settlement-related nuisance, the worst option is a general scheme for personal income tax and corporate income tax that is settled based on books of account.

It should be noted, however, that the assessment of formal obligations should take into account more than just income tax. Indeed, the entrepreneur's obligations related to tax settlements are performed along with other record keeping and reporting obligations, primarily those concerning VAT and employee settlements. Consequently, simplifications applicable to lump-sum taxation schemes may not be valid if a taxable person must still settle VAT and employees.

On the other hand, record keeping costs make an essential factor, if a taxable person has a choice between accounting records and a cheaper and simpler method, i.e. the tax book of revenue and expenditure.

Tax risk

An important criterion in the taxation scheme evaluation is the tax risk. It should be assumed that a tangible value for any taxable person is tax certainty. Certainty, and therefore predictability, of the tax obligation and thus the amount of the tax liability.

A taxable person expects instantiation of the tax obligation (i.e. determination whether the tax should be paid at all, and if so, at what time) and of the tax liability (i.e. determination of the tax amount). If a taxable person can be certain that their tax approach is correct, they can plan business activities and avoid fiscal penal sanctions.

The tax risk depends on the tax determination method, the scope of available tax reliefs and deductions, and the form of record keeping. In view of these factors, the least risky taxation scheme is the "tax card" scheme, followed by the lump-sum tax on registered revenue. The most risky is the general scheme with the tax settled based on accounting records.

The tax risk issue is so important due to its immeasurable nature and the fact that the taxable person must resolve the dilemma of how to minimize both the risk and the tax payments.

More often than not, however, the better the tax reduction opportunities, the higher the tax risk.

Ability to influence the tax burden

For many taxable persons, an important criterion in selecting a taxation scheme will be the ability to influence the tax burden, especially on tax payments. Tax flexibility reflects the degree of a taxable person's freedom in the fulfilment of the tribute obligation. Such freedom should be analysed from at least two points of view. Firstly, tax flexibility expresses itself in the possibility of a rapid (i.e. mid-tax year) transition to another taxation scheme. Secondly, within individual taxation schemes, an entrepreneur can to a greater or lesser degree control the moment of occurrence and the amount of tax payments.

Transition to another taxation scheme may also take place by ending the current and starting a new business activity. If the scope of the "new" business is identical or very similar to the previous one, then the tax authorities may interpret this transformation as an attempt to circumvent law only to obtain tax benefits. Therefore, changing the taxation scheme by liquidation is a risky option.

In the case of individuals, a mid-year change in the taxation scheme may occur if a situation is brought about when the person loses the right to use a given scheme. For instance, a taxable person loses the right to use the "tax card" scheme if they expand the scope of business, or their headcount exceeds the limit. Business expansion and selling to a current or former employer are situations where a taxable person must resign from the lump-sum tax on registered revenue.

Similarly, a taxable person loses the right to apply the flat-rate tax scheme if they sell to a current or former employer.

In other words, taxable persons may push their business in such a direction that they will lose the right to use previously selected taxation schemes: "tax card", lump-sum amount on registered revenue or the flat-rate tax. Only in the case of progressive tax is it not possible to switch to another scheme during the year.

Anticipated amounts of tax to pay

The main criterion for selection of an income tax scheme consists of the anticipated amounts of tax to pay in a given settlement period. This period is usually the time until the end of a calendar year (or a selected financial year in the case of legal persons).

The lower the income tax payments, the more advantageous the taxation scheme. Individual taxes are calculated according to different formulas, that is why their final amount depends on the individual circumstances of the taxable person. Therefore, it is impossible to indicate which scheme would be always the favourable or always the unfavourable one. In one case, the flat-rate personal income tax will be an advantageous choice, while in another case it will be utterly unprofitable. However, any taxation scheme may turn out to be beneficial if only certain conditions are satisfied.

For a taxable person deciding on the choice of a taxation scheme, it is therefore crucial to establish the profitability factors of individual taxes and how to handle the tax policy so as to establish the tax at potentially the lowest level.

The amount of tax is determined by disclosed revenue and expenditure, deductions from a taxable base, deductions from the tax itself, and, last but not least, tax rates.

While analysing tax payments, one should therefore take into account the expected economic situation of the enterprise (revenue, expenditure, investments), possible ways of its tax recognition (disclosing revenue and expenditure), as well as applicable tax deductions.

A factor of great importance is the taxable person's personal situation, especially their obligations in terms of insurance contributions, non-business sources of income, the right to tax reliefs, including as part of acquired rights, as well as the right to file tax returns with the spouse or children.

So ultimately, the amount of tax depends on the individual circumstances of both the enterprise and the taxable person themselves.

Revenue from business activities

Taxable persons conducting their business under to the general taxation scheme or the flat-rate tax scheme record their revenue and expenditure in the tax book of revenue and expenditure or keep full books of account in accordance with accounting regulations.

Pursuant to Article 14 para. 1 of the Act on Personal Income Tax, revenue from non-agricultural business activities is understood as amounts due, even if not actually received, less the value of goods returned, and the rebates and cash discounts granted. In the case of taxable persons selling goods and services subject to tax on goods and services, sales revenue is understood as the revenue reduced by the output tax on goods and services.

This provision is an exception to a general rule concerning the principles of determining the amount of revenue contained in Article 11 para. 1, according to which the revenue consists of money and monetary assets received by or made available to the taxable person during a calendar year, as well as the value of benefits received in kind and other free performances.

In the case of business revenue, the revenue day is the day when a receivable originated rather than the day when a taxable person received money for the product sold or the service rendered. This solution can lead to a situation in which a taxable person has not received any payment from their contractor, but will still be obliged to pay income tax. Here we deal with the principle known as the accrual principle.

With respect to business revenue, the accrual principle does not apply to revenue in the form of interest on borrowings granted, cash at bank and contractual indemnities received, as they are all governed by the cash-basis principle.

If a taxable person sells goods (renders services) that are subject to tax on goods and services, then their revenue is the amount excluding the output tax on goods and services.

According to the VAT Act, the taxable base is the turnover, i.e. the amount due against sales, less the amount of output tax. Output tax on goods and services is to be paid by a taxable person pursuing taxable activities at the amount resulting from the application of the appropriate rate to the taxable base. While paying tax on goods and services, a taxable person is entitled to reduce the amount of output tax by the amount of input tax (i.e. the tax on purchase of goods and services).

A rebate and a cash discount are price reductions. A rebate is granted based on the subject (for specific customer categories), the object (e.g. form of sales), or in connection with actual or anticipated damage suffered by a counterparty (e.g. in connection with sales of lower grade or defective products). Cash discount applies when payment occurs in the form that is more convenient for the seller, e.g. in cash or at an earlier date than the date specified in the contract.*

Special categories of business revenue

Business revenue is not limited to trade receivables. The array of tax revenue items is in fact quite broad.

Thus the revenue derived from a business source also includes the following:

1) Revenue from transfer for consideration of assets that are used for business purposes or for management of special branches of agricultural production:

    a) which are fixed assets;
    b) whose initial recognition is below 3500 PLN, but higher than 1500 PLN ("equipment");
    c) which are intangible assets.

This means that the sale of company assets is business revenue. On the other hand, revenue from non-agricultural business activities does not include revenue from transfer for consideration of residential premises and buildings (and their parts) that are used for business purposes.

2) Subsidies, grants, additional payments and other gratuitous performances received to cover the costs, or as a reimbursement of expenses, except when such revenue is associated with receiving, purchase or independent development of fixed or intangible assets – it is because of the fact that in this case the entrepreneur does not recognise depreciation/amortisation allowances on that part of the asset which was financed in the manner indicated above.

Subsidies and grants are monetary benefits which constitute expenses from the state or gmina budget, which are unilaterally determined by the granting entity, non-refundable and granted without consideration.

3) Foreign exchange differences.

Foreign exchange gains increase taxable revenue increase, whereas foreign exchange losses increase the revenue expenditure.

4) Contractual indemnities received.

Contractual indemnities are intended as compensation for damage in case of non-performance or improper performance of the obligation. Only received contractual indemnities are considered revenue (it is not enough for the indemnity to be due).

5) Interest on cash at bank, held in the context of business activities.

Interest on a taxable person's savings deposits (unrelated to business) constitutes capital gains income and is taxed at a flat rate of 19% (the tax known after a former Minister of Finance, Marek Belka as "Belka's tax", and deducted by banks).

On the other hand, interest on corporate accounts of the entrepreneur is recognised as business revenue.

6) Amount of written-off or time-barred liabilities.

The exception here consists of amounts equivalent to liabilities written off, including borrowings (loans) written off, if writing-off of such liabilities is related to bankruptcy proceedings or a possible composition with creditors within the meaning of bankruptcy and restructuring law, including against loans (borrowings) taken out – if such liabilities are written off, no revenue occurs.

The value of other benefits associated with writing-off of overdue liabilities, including borrowings from the Labour Fund that have been written off will constitute revenue.

Written-off and time-barred liabilities may be considered revenue because they increase the taxable person's ability to pay tax. Such a condition is not met by liabilities written off in connection with bankruptcy proceedings. Therefore, it is only justified not to recognise them as revenue.

7) Value of returned claims that have been recognised under revenue in line with legal regulation.

If in accordance with legal regulations, a taxable person recognised an uncollected claim under revenue expenditure, and then the claim was paid, then it should be added to revenue.

8) Amount of tax on goods and services:

   a) not recognised in the initial value of fixed and intangible assets that are subject to depreciation/amortisation; or
   b) concerning other property or rights other than fixed or intangible assets.

   - in the part in which the adjustment has been made resulting in an increase of the tax deducted in accordance with Article 91 of the VAT Act;

In accordance with that provision of the VAT Act, a taxable person is entitled to include undeducted tax on goods and services under revenue expenditure. If a taxable person subsequently adjusts VAT in such a way that the deducted tax amount increases, the amount of the tax resulting in an overstatement of expenditure should be included under revenue (in other words, expenditure is not adjusted).

Example:

In 2010 a taxable person bought for business purposes a passenger car with type approval as a goods vehicle (known colloquially in Polish as "a car with a grille partition") for 55,454.55 PLN gross (VAT: 10,000 PLN). They only deducted 60% from the input VAT, i.e. 6000 PLN.

In May 2011, following a favourable judgment by the ECJ and a new interpretation of the tax regulations by the Polish Ministry of Finance, the taxable person corrected their VAT return and deducted the entire tax (which resulted in an overpayment of VAT in the amount of 4000 PLN). At the same time, in May 2011 the taxable person will recognise the amount under their business revenue.

9) Revenue earned in connection with a borrowing (loan) returned or obtained, if the borrowing (loan) was indexed using an FX rate, where:

   a) the lender receives cash representing a repayment of the principal at the amount higher than the amount of the borrowing (loan) granted – at the difference between the amount of the returned principal and the amount of the borrowing (loan) granted;
   b) the borrower returns, as part of the borrowing (loan) repayment, cash representing a repayment of the principal at an amount lower than the amount of the borrowing (loan) received – at the difference between the amount of the borrowing (loan) received and the amount of the returned principal.

While discussing revenue expenditure, we mentioned that the expenditure comprises a "loss" related to indexation of the borrowing with an FX rate. By analogy, any "gain" from such indexation will be a revenue item.

10) Value of benefits received in kind and other free performances.

Typical examples of benefits in kind and free performances that are considered revenue include:

- market value of interest, if an interest-free borrowing is obtained (or a difference between interest paid and the market interest in the case of borrowings with interest more favourable than market interest);
- rewards associated with 'sales with a bonus' as received by taxable persons engaged in business activities (note: sometimes such a reward may be granted to an employee, not an entrepreneur, then it will be considered the employee's revenue).

There is an exception to that rule: pursuant to Article 21 para. 1 item 125, the value of benefits in kind and other free performances received from persons who fall into tax group I or II within the meaning of the regulations concerning inheritance and donations tax is tax free (the exemption does not apply to benefits received on the basis of employment and related relationships).

Tax group I includes: spouses, descendants, ascendants, stepchildren, sons-in-law, daughters-in-law, siblings, stepfathers, stepmothers, and parents-in-law. On the other hand, according to the legislator, tax group II includes: descendants of siblings; siblings of parents; descendants and spouses of stepchildren; spouses of siblings and siblings of spouses; spouses of spouses' siblings; and spouses of other descendants. What is important is that parents within the meaning of that Act include adoptive parents, and descendants also include adoptees and their descendants.

11) Revenue from rental, subletting, lease, sublease and other contracts of a similar nature concerning assets related to a business activity.
12) Compensations received for damage to assets related to a business activity or management of special branches of agricultural production.
13) Revenue from transfer for consideration of the following assets:

    a) remaining at the date of liquidation of a self-employed business;
    b) received in connection with liquidation of a non-incorporated company or withdrawal of a shareholder from such company.

If a notice is submitted to the head of a tax office on liquidation of a non-incorporated company or on withdrawal of a shareholder from such company, a list is drawn up of assets remaining as at the date of liquidation of the business or as at the date of the shareholder's withdrawal from such company (Article 24 paras. 3a-3e of the PIT Act).

The list should include at least the following information: ordinal number, specification (name) of the asset, asset acquisition date, amount spent on acquisition of the asset, amount spent on acquisition of the asset and recognised under revenue expenditure, and amount of funds due and paid to shareholders against their interest in a non-incorporated company as at the date of withdrawal or liquidation.

At the same time, no revenue arises if between the first day of the month following the month in which the following took place: liquidation of a self-employed business, liquidation of a non-incorporated company, or withdrawal of a shareholder from such company – and from the date of their transfer for consideration 6 years have passed, and the transfer for consideration is not effected as part of a business activity.

Example:

John pursues a business activity in which a fixed asset is a passenger car.

He closed down his business with effect from 1 December 2012. Since then he had been using the car for private purposes, but on 1 March 2013, he sold it for 10,000 PLN.

Although John is no longer in business, revenue from the sales concerned constitutes business revenue. This is because the sales were completed within 6 years of the closing date of his business. Therefore, John will have to pay advance tax and account for the corresponding income in his annual tax return for 2013.

If a sale transaction took place after 6 years, no revenue would apply.

Exemptions from revenue

The Income Tax Act contains a catalogue of performances that do not constitute revenue (note: this is for income tax purposes; revenue is established quite differently for VAT purposes).

So revenue does not include, among other things:

a) payments collected or receivables accrued relative to supplies of goods and services which will be performed in subsequent reporting periods, as well as borrowings and loans obtained and borrowings returned, except for capitalised interest on such borrowings;

Advance payments are not a revenue item. Revenue will only occur when a relevant performance is completed. Similarly, borrowings obtained are not considered revenue either.

b) interest accrued but not received on receivables, including borrowings granted;

Interest becomes a revenue or expenditure item when it is actually paid. Therefore, accrued but not received interest is not revenue.

c) refunded, redeemed or abandoned taxes and charges which constitute income of the state budget or local government budgets, not recognised under revenue expenditure;
d) other reimbursed expenses, not recognised under revenue expenditure.

Business activity of foreigners

Finally, let us check what rules apply to foreigners who would like to start a business activity in Poland.

In accordance with Article 13 of the Act on Freedom of Economic Activity, foreign persons from Member States of the European Union, Member States of the European Free Trade Association (EFTA) – parties to the Agreement on the European Economic Area (EEA) and foreign persons from states that are not a party to the EEA Agreement that may benefit from the freedom of establishment on the basis of agreements between those states and the European Community and its Member States may undertake and carry out a business activity on the same terms as Polish citizens.

Citizens of states other than mentioned above, who:

- have in Poland:
    - a settlement permit;
    - an EC long-term residence permit;
    - a fixed period residence permit;
    - a fixed period residence permit granted to a member of the family staying within the territory of the Republic of Poland, or staying in that territory for the purpose of family reunification;
    - a refugee status;
    - subsidiary protection;
    - a discretionary leave to remain;

  - a fixed period residence permit, and they are married to a Polish citizen residing in Poland;
  - a visa referred to in Article 61 para. 3 or Article 71a para. 3 of the Act on Foreigners dated 13 June 2003, if, prior to the issue of a visa, they have been entitled to take up and pursue a business activity;
- enjoy a temporary protection in Poland;
- have a valid Card of the Pole;
- are a family member within the meaning of Article 2 item 4 of the Act of 14 July 2006 on Entry into the Territory of the Republic of Poland, Residence and Exit from its Territory of EU Citizens and Members of their Families, joining citizens of the states referred to in para. 1 or staying with them;
- may undertake and pursue a business activity in Poland on the same terms as Polish citizens.

All other foreign persons (not listed above) have the right to take up and pursue a business activity only in the form of the following companies: limited partnership, limited partnership on shares, limited liability company and joint stock company; they may also join such companies and take hold of or acquire interest in them, unless international agreements provide otherwise.

Summary

A person who intends to take up a business activity has a selection of taxation schemes from which to choose.

These schemes differ in terms of obligations related to determination of a taxable base, keeping of accounting records and, last but not least, the amount of tax to pay.

In the general taxation scheme and the flat-rate tax scheme for businesses, the obligations are more or less the same. Still, the amount of tax is determined in different ways, which obviously influences the tax burden.

PERSONAL INCOME TAX. REVENUE EXPENDITURE:

EXPENSES NOT CONSIDERED REVENUE EXPENDITURE

We should pay attention to the fact that in accordance with the statutory definition, revenue expenditure is expenditure incurred to generate revenue or to maintain or secure a source of revenue, except for the expenditure listed in the Act.

Both Income Tax Acts include a catalogue of expenditure items that will not be considered revenue expenditure; in the PIT Act the list appears in Article 23, and in the CIT Act in Article 16 para. 1. As we know, only entrepreneurs have the right to apply expenditure at its actual amount. In the case of revenue from other sources, lump-sum expenditure is typically applicable, in the amount specified by the legislator.

Therefore, a negative catalogue of expenditure items refers in principle only to entrepreneurs, and is almost identical in both Acts.

The catalogue is extensive and comprises expenses of a different character. Today, we will have a look at such "prohibited" expenses that the entrepreneurs must deal with most frequently, and which therefore cause many problems and much controversy.

In an attempt to systematize this catalogue, we can say that the expenses that are not tax expenditure take the form of:

1) expenses on acquisition of tangible, intangible and financial components of non-current assets, at the moment when they are incurred;
2) expenses related to the discharge by a taxable person of their liabilities towards creditors, and losses related to the taxable person's debtors defaulting on their obligations;
3) expenses being financial sanctions;
4) expenses related to the settlement of liabilities towards the State Treasury;
5) other expenses of a varied nature.

Expenses on acquisition of tangible, intangible and financial components of non-current assets, at the moment when they are incurred

In one of the chapters we discuss a rather unusual expense, which is depreciation/amortisation.

Depreciation or amortisation is a monetary expression of the progressive wear and tear of assets that are used in a business, rented and leased.

If an entrepreneur buys an asset to be used for business purposes, and the asset will be used over longer term (above one year), they cannot recognise relevant expenses as revenue expenditure on a one-off basis. On the contrary, the expense will be debited to tax expenditure throughout the asset's useful life, by means of depreciation/amortisation allowances.

Example:

An entrepreneur buys a car for business use for 50,000 PLN. He cannot recognise this expense under expenditure on a one-basis, but is obliged to use depreciation allowances.

In accordance with legal regulations, the annual depreciation rate for cars is 20%, which means that the expense on the car's purchase will be spread over a period of 5 years.

So any expenses on acquisition of tangible, intangible and financial components of non-current assets do not become an expenditure item when incurred but become one gradually, by means of depreciation/amortisation allowances.

Legal regulations also provide for situations where depreciation/amortisation allowances are not considered revenue expenditure. Therefore, the following will not be considered revenue expenditure:

1) Depreciation allowances on a passenger car, in that part of the car value that exceeds the equivalent of 20,000 EUR.

Tax authorities are suspicious of entrepreneurs who use passenger cars for business purposes. In a sense, tax regulations assume that an entrepreneur uses such car not only for business but also for private purposes, so we have here a number of limitations in recognition of expenses as revenue expenditure, or in VAT deductions.

One can also come to the conclusion that primary "suspects" are entrepreneurs buying cars worth more than 20,000 EUR. Taxable persons that use such cars as a fixed asset may not recognise under revenue expenditure those depreciation allowances that refer to the "surplus" over the value of 20,000 EUR.

This means that before they start to recognise depreciation allowances on a passenger car, a taxable person should first verify whether the car value does not exceed the equivalent of 20,000 EUR. If it does, it is necessary to calculate what portion of a depreciation allowance will not be tax expenditure.

Example:

At the date when the car is accepted for use, the equivalent of 20,000 EUR is 80,000 PLN, and the car's initial recognition amounts to 200,000 PLN.

If we apply the depreciation rate of 20%, the annual depreciation would amount to 40,000 PLN. However, the tax expenditure for the year will only amount to 16,000 PLN (20% × 80,000 PLN). Thus, 24,000 PLN will be the amount excluded from revenue expenditure.

2) Depreciation/amortisation allowances on fixed and intangible assets, on that part of their value which corresponds to the expenses incurred on their acquisition or independent development that has been deducted from the taxable base in income tax, or has been refunded to a taxable person in any form whatsoever.

So revenue expenditure does not include depreciation/amortisation allowances on fixed and intangible assets on that part of their value that has been refunded to a taxable person in any form whatsoever or financed with the revenue which was subject to tax exemption.

Example:

A taxable person buys a fixed asset for 100,000 PLN net. The depreciation rate is 20%. After a year, the taxable person receives a subsidy from the European Union to finance 40% of the fixed asset purchase (i.e. 40,000 PLN). How should the situation be reflected in the taxable person's expenditure settlements?

Since the taxable person received a partial refund for the asset's value (i.e. 40,000 PLN), depreciation allowances on that part cannot be recognised as revenue expenditure. If we assume that in the first year the taxable person recognised allowances on the entire value of the asset, then in the first year the allowances in question reached 20,000 PLN (100,000 PLN x 20%).

In connection with the subsidy received, 40% of that amount will not be considered expenditure. Therefore, the taxable person should adjust their expenditure by 8000 PLN (20,000 PLN x 40%), and in subsequent years recognise depreciation allowances of 60,000 PLN, i.e. 12,000/year.

3) Depreciation/amortisation allowances on the initial value of fixed and intangible assets:

   a) that were acquired free of charge, with the exception of those acquired through inheritance or donation, if:
      - such acquisition does not constitute revenue derived from a free-of-charge receipt of property or rights; or
      - corresponding income is exempt from income tax, or
      - the acquisition constitutes income on which tax collection was abandoned pursuant to separate regulations;
   b) if, before 1 January 1995 they had been acquired but not recognised under fixed or intangible assets;
   c) transferred for a free-of-charge use – for the months in which such assets remained under free use.

To put the above provision in simple terms, we can say that no depreciation allowances must be recognised on fixed assets that have been received by a taxable person for free, and such acquisition did not give rise to tax revenue, or such revenue was tax-free.

Example:

It was mentioned recently that an unemployed person can receive from a Starost (via a job centre) a one-off allowance to start a business activity in a contractual amount not higher than 6 times the average salary.

These funds are tax exempt.

So if an entrepreneur uses these funds to buy a fixed asset for business purposes, they will not be able to depreciate it for tax purposes.

Expenses related to the discharge by a taxable person of their liabilities towards creditors, and losses related to the taxable person's debtors defaulting on their obligations

This group of expenses includes various expenditures related to the servicing of borrowings and claims. And so, the following will not be considered tax expenditure:

1) Expenses on:

   a) repayment of borrowings (loans), excluding capitalised interest on such borrowings (loans), on the proviso that revenue expenditure consists of expenses on the repayment of the borrowing (loan) where the borrowing (loan) was indexed with an FX rate, if:

      - the borrower returns, as part of the borrowing (loan) repayment, the principal amount higher than the amount of the borrowing (loan) received – at the difference between the amount of the returned principal and the amount of the borrowing (loan) received;
      - the lender receives cash representing a repayment of the principal at an amount lower than the amount of the borrowing (loan) granted – at the difference between the amount of the borrowing (loan) granted and the amount of the returned principal;

b) repayment of other liabilities, including in respect of guarantees and sureties granted.

On the whole, borrowings are tax neutral. In other words, borrowings obtained are not revenue (they must be repaid after all) and, on the other hand, the repayment of a borrowing is not expenditure.

However, the tax liability arises in connection with interest: interest received is the lender's revenue whereas interest paid is the borrower's expenditure.

The legislator has also provided for a situation where the repayment of the principal part of the borrowing results in itself in a gain or loss (because the borrowing was indexed with an FX rate), representing accordingly a revenue or expenditure item.

Example:

Elisabeth lends Joan 1000 EUR, but they agree that the borrowing will be paid and returned in its current equivalent in PLN, calculated according to the average exchange rate of the National Bank of Poland (NBP).

The borrowing is granted on 5 January 2012. At that date, the EUR exchange rate amounts to 4.5135, so Elisabeth lends 4513 PLN. Joan returns the borrowing on 4 January 2013. At that date, the exchange rate amounts to 4.1248, so the amount returned amounts to 4125 PLN.

As a result of indexation, Elisabeth records a "loss" on the borrowing equal to 388 PLN. In accordance with legal regulations, she will be able to include the amount as expenditure.

In the opposite situation, that is, if on the borrowing repayment date, the EUR exchange rate is lower than on the day it was granted, it would be the borrower (Joan) who must recognise expenditure.

2) Borrowings granted, including borrowings lost.

As we have just mentioned, borrowings are tax neutral: the granting and the repayment of a borrowing are neither revenue nor expenditure. Hence, borrowings lost will not be expenditure either.

3) Interest accrued but not paid or remitted concerning liabilities, including interest on borrowings (loans).

Only interest paid is considered expenditure. Thus, interest that has not been paid by a taxable person will not be considered expenditure. Not only is the interest remitted not an expenditure item but it will most frequently be considered revenue.

4) Borrowings written off, provided that this is unrelated to bankruptcy proceedings or a possible composition with creditors within the meaning of bankruptcy and restructuring law.
5) Claims remitted, except for those which have previously been accrued as revenue receivable.

Speaking of revenue, we have mentioned that in the case of a business activity, the accrual principle applies, i.e. tax revenue is revenue receivable, even if it has not been obtained yet. It can happen that a taxable person does not receive such revenue from a debtor, and therefore decides to remit it. For the remittance to be effective, the debtor must agree to be released from debt (which may be not so obvious concerning tax regulations).

Remittance of a claim that has been posted as revenue will constitute an item of tax expenditure.

Example:

ABA co. sells goods to VETO co. Unfortunately, for reasons related to customer solvency problems and the unfavourable prospect of collecting the receivable, ABA decides to remit the overdue amount (the debtor agrees to be released from debt).

As a result, ABA has the right to recognise the remitted claim as revenue expenditure.

6) Claims written off as time-barred.

There is no single common limitation period for all claims. A general rule is that if a specific provision does not provide otherwise then the period of limitation is 10 years, while for claims concerning periodical performances and claims related to the conduct of business the period is 3 years. The limitation period depends on the type of claim.

In any case, if a claim becomes time-barred, the debtor can legally refuse to repay the debt. What is more, the creditor having an uncollected claim will not be able to recognise it under tax expenditure.

7) Claims written-off as uncollectible, except for those which have previously been accrued as revenue receivable and whose non-collectability has been disclosed prima facie.

The claims discussed here are claims whose non-collectability has been documented with:

- a non-collectability resolution, acknowledged by the creditor as corresponding to the facts, issued by a competent authority responsible for enforcement proceedings; or
- a court decision:

to dismiss a petition for bankruptcy involving the liquidation of assets, if the insolvent debtor's assets are insufficient to cover the costs of the proceedings;

or

to discontinue the bankruptcy proceedings involving the liquidation of assets when the circumstance referred to in the preceding item occurs; or

to complete the bankruptcy proceedings involving the liquidation of assets; or a protocol drawn up by a taxable person, stating that the expected costs of the proceedings and enforcement associated with the assertion of a claim would be equal to or higher than the amount claimed.

Example:

Mr. Smith operates a business and has a claim of 500 PLN against Fraudstery Ltd. Despite repeated reminders, the debtor does not repay their liability.

How can Mr. Smith recognise the claim concerned under revenue expenditure?

To enforce such a claim through the court and enforcement proceedings would probably be unprofitable for Mr. Smith, as costs of such proceedings could be higher than the claim amount.

If this is the case, then following the preparation of a protocol from which it will be apparent that the costs of the proceedings and enforcement are higher than the arrears, Mr. Smith will be able to recognise the claim under revenue expenditure.

We should remember, however, that should a debtor return the debt once the claim has been recognised under revenue expenditure, then the claim should be re-stated as revenue.

Expenses being financial sanctions

Running a business is subject to numerous laws and regulations to which entrepreneurs are obliged to adhere. If they breach such legal provisions, they often become exposed to sanctions of various nature. These can be legal sanctions or sanctions imposed under other regulations, such as contracts with contractors.

In tax regulations, we have a principle that all penalties and other sanctions that are imposed on the entrepreneur are not revenue expenditure.

If the expenses incurred in connection with entrepreneur's negligence were to be revenue expenditure, then: first, it could be considered that the state budget partially reimburses the entrepreneur for such expenses (by partially resigning from the tax due), and secondly, it would put defaulting entrepreneurs in a privileged position compared to entrepreneurs that diligently perform their obligations. Thus, sanctions and penalties imposed on the entrepreneur are not considered revenue expenditure.

Among these expenses, we find the following:

1) Enforcement expenditure related to defaults.
2) Fines and pecuniary penalties awarded in criminal, criminal fiscal and administrative proceedings and in cases related to petty offences, as well as interest on such fines and penalties.
3) Penalties, fees and damages, and interest on such liabilities in respect of:
   a) non-compliance with environmental regulations;
   b) failure to implement any orders of competent supervision and inspection authorities regarding negligence in the field of occupational health and safety;
4) Default interest on overdue payments of budgetary dues and other charges, to which the provisions of the Tax Code of 29 August 1997 apply;
5) Contractual indemnities and damages relative to defects in goods delivered or work and services performed, and delay in delivery of goods free of defects, or delay in removal of defects in goods or work and services performed;

6) The amount of additional annual fees for non-development or non-improvement of land within a specified time-limit, pursuant to the provisions on real property management;
7) Sanction fees which, according to separate regulations, are to be paid to the state budget or local government budgets;
8) One-time compensations for accidents at work and occupational diseases in the amount specified by a competent minister, and an additional insurance contribution, if deterioration of working conditions is ascertained;
9) Additional product fee referred to in Article 17 para. 2 of the Act of 11 May 2001 on the Obligations of Entrepreneurs in the field of Management of Certain Waste and the Product Fee and Deposit Fee, on the proviso that revenue expenditure is the product fee referred to in Article 12 para. 2 of the Act.

Expenses related to the settlement of tax liabilities

A general rule is that taxes paid may not be revenue expenditure. However, there are some exceptions to that rule, when a given tax under certain conditions may actually be considered revenue expenditure.

The following taxes are not considered tax expenditure:

- income tax;
- inheritance and donations tax;
- losses incurred as a result of shrinkage of excise goods that are not subject to excise tax exemption, and excise duty on such shrinkage.

Exceptions concerning tax on goods and services

A general rule is that VAT is not revenue expenditure.

This means that expenses are debited to costs in the net amount: this is because VAT is settled on the basis of VAT regulations. There are, however, some exceptions here.

Revenue expenditure may include the input tax, i.e. tax that we pay as part of the price of goods and services purchased. A taxable person that is not subject to VAT regulations (because a subjective exemption applies to them due to, for example, the turnover achieved, or an objective exemption is applicable (a given business activity is not subject to VAT)) may recognise their gross expenses (i.e. VAT-inclusive amount) under revenue expenditure.

Input tax may also be revenue expenditure in that part for which, in accordance with the provisions on the tax on goods and services, a taxable person is not entitled to a reduction or a refund of the difference in tax on goods and services (except where the input VAT increases the value of a fixed or intangible asset – here the input tax becomes an expenditure item by means of depreciation/amortisation allowances).

Example:

VAT payers that use passenger cars for their business are not entitled to deduct VAT included in the price of fuel.

Therefore, the input VAT that the taxable person cannot deduct under VAT regulations, may be recognised under revenue expenditure provided, of course, that the expense is connected to revenue.

Under certain conditions, the output tax, i.e. VAT that is added by a VAT payer to their own invoices, may be a tax expenditure item too.

Firstly, the input tax may become tax expenditure in the case of service imports and intra-Community acquisition of goods.

When a VAT payer buys a product or service from a contractor from the European Union, they have the obligation to settle VAT. The seller does not disclose VAT in their invoice but a Polish buyer adds the tax and pays it to a tax office. In most cases such an operation is tax-neutral, because the output tax becomes at the same time the input tax. In other words, we disclose the tax simultaneously as the tax to pay and the tax for the refund. However, it will not always be the case. Sometimes a taxable person is not entitled to deduct VAT – for example, in situations where the acquired good and service are used to provide tax-free services or sell tax-free goods. Then the output tax which is not the input tax will be revenue expenditure. On the other hand, tax expenditure will not include the output tax in excess of the amount of tax on purchase of such goods and services, which could be the input tax within the meaning of the provisions governing tax on goods and services.

Secondly, the input tax may be an expenditure item if a taxable person transfers or consumes goods or provides services for entertainment and advertising purposes, with such tax calculated in accordance with separate regulations.

Expenditure may also include the input tax on goods supplied free of charge, calculated in accordance with separate regulations, where the sole condition for the supply is the previous acquisition by a receiving party of goods or services from the supplying party in a specific quantity or of a specific value.

Tax expenditure will also include the amount of tax on goods and service not included in the initial value of fixed and intangible assets that are subject to depreciation/amortisation in accordance with Article 22a-22o, or concerning other property or rights other than fixed or intangible assets that are subject to such depreciation/amortisation – in the part in which the adjustment has been made resulting in a decrease of the tax deducted in accordance with Article 91 of the VAT Act.

Example:

A taxable person buys for business purposes a passenger car with type approval as a goods vehicle (known colloquially in Polish as "a car with a grille partition") and deducts 100% VAT. As a result, they adopt the net amount as the initial value for the fixed asset's depreciation purposes.

After some time, the taxable person realises that they have made a mistake, because they had no right to deduct 100% VAT, but only 60% (as is the case with "ordinary" passenger cars). Consequently, they correct the VAT settlements and pay the tax of 40%. At the same time, in accordance with the provision quoted above, the initial recognition of the fixed asset is not adjusted here.

Other expenses that are not revenue expenditure

In addition to the above expenses, a "negative catalogue of expenditure" comprises several items, which for taxable persons have been a nuisance for years. The last group of expenditure items which are not treated as revenue expenditure consists of miscellaneous expenses.

Hence, the following will not be considered revenue expenditure:

1) Entertainment expenditure, in particular on catering services and purchase of food and beverages, including alcoholic beverages.

This is one of the more dubious constraints applicable to expenditure. It is because the legislator has assumed that the entertainment expenses of a taxable person cannot be treated as revenue expenditure. But the problem is that... we do not know exactly what "entertainment" is. There is no statutory definition of the term, and a dictionary entry is all the more confusing because it is an ambiguous concept.

In recent years, tax authorities have assumed the following for the purposes of interpretation of the limitation concerned:

"(…) entertainment concerns representing a taxable person (company) entailing grandeur and sophistication, in order make the best possible impression. So the "entertainment" concept includes such activities of a taxable person which aim to create (reinforce) an appropriate image of the company. The appropriate image is such "depiction of the entrepreneur" shaped by means of entertainment spending which translates into purchases of its goods (services). A conscious development of the company's appropriate image is therefore meant to create such perception of the entrepreneur which will arouse positive associations among third parties".

In fact, this definition is far from perfect. Disputes usually occur in a situation where a tax authority classifies as entertainment expenses (with entertainment understood as entailing grandeur and sophistication) such expenses that are standard for taxable persons operating in a given industry.

Example:

A company leases an aircraft to be used for business travel by the CEO and other persons. The tax authorities decide that it is an entertainment expenditure and as such may not be a revenue expenditure.

A Voivodeship Administrative Court disagrees with that position and states as follows: "In the opinion of the Court, recognition of the entire expenditure related to the lease and operation of the aircraft under entertainment expenses is legally unfounded, as it is only based on the conviction that air travel is "a luxurious and sophisticated service that may add to the company prestige".

It can be inferred from the Applicant's explanations that the plane was leased for business travel of the CEO and other employees of the company. Expenses related to business travel are the enterprise's operating expenditure and it is irrelevant to the assessment of the nature of such expenditure concerning what means of transport is used. Whether a company uses a worn-out car or a modern aircraft for its own transportation needs cannot be a matter for expenditure classification" (judgment of the Voivodeship Administrative Court in Warsaw of 14 April 2004, ref.: III SA 2893/2002).

Among entertainment-related disputes, the most widespread are those related to meals (catering services).

Sometimes, tax authorities consider that legal regulations prohibit recognition under revenue expenditure of all meal expenses, including in particular the amounts spent on alcoholic beverages. The legal provision, however, clearly indicates such meal expenses which are considered entertainment expenses.

A prominent issue in such disputes is the question of whether an expense associated with inviting a contractor to a restaurant for dinner (for instance to have business talks in a relaxing atmosphere) can be considered a tax expenditure item or not. In spite of the fact that the expense is or may be related to revenue, tax authorities argue that we deal with entertainment expenses here.

Unfortunately, court judgments on this matter are ambiguous.

2) Unpaid contributions to the Social Insurance Institution (ZUS).

Surely, this exclusion is logical and undisputed. Revenue expenditure may include social insurance contributions but only those that have been paid (it is not enough for the contribution to be due).

3) Membership fees for organisations to which a taxable person is not obliged to belong, with the exception of:

   a) payments made by taxable persons operating their business in the field of tourism, leisure, sports and recreation for the Polish Tourist Organisation (POT);
   b) membership fees for organisations associating entrepreneurs and employers, which operate under separate laws – up to a total amount not exceeding in a tax year the amount corresponding to 0.15% of salaries paid in the previous tax year, which are the basis for assessment of social security contributions; if an entrepreneur did not pay salaries, the amount of membership fees that may be recognised under revenue expenditure in a tax year may not exceed the equivalent of 114 PLN.

Revenue expenditure includes membership fees for organisations to which a taxable person is obliged to belong (e.g. because of their trade or profession). In contrast, membership fees for organisations other than specifically listed in the legislation as exceptions are not considered tax expenditure.

4) Value of a taxable person's own work, as well as work of their spouse and minor children, and in the case of business in the form of a civil partnership or a commercial partnership – also including work of partners' spouses and minor children.

Pursuant to personal income tax regulations, taxable persons are partners in a partnership and not partnerships themselves (the Ministry of Finance plans to extend corporate income tax to limited partnerships on shares – the announced change will be effective starting from 1 January 2014). As a result, the value of work (regardless of the form of service) provided by a taxable person, their spouse and minor children is not a revenue expenditure item for any of taxable persons.

It should be noted, however, that this exclusion does not extend to the value of work of the remaining partners. This means that the remuneration paid to one partner in the company under a contract of employment is not a revenue expenditure item only for the taxable person concerned. Consequently, nothing stands in the way of recognising such remuneration among revenue expenditure of the remaining partners – in proportion to their interest in the company profit (shareholding).

What is also important is the fact that work performed cannot be associated with representation of the partnership or management of its affairs, or stem from the obligations set out in the partnership foundation deed (cf. resolution of the Supreme Court of 14 January 1993, ref.: II UZP 21/92, OSNC 1993/5, item 69).

This rule does not apply in the case of partners' spouses and minor children – the value of their work cannot be included in revenue expenditure of all partners in the partnership.

Example:

Simon and Gordon are partners in a general partnership, and each of them holds a 50% share in profit.

Each of the partners is employed in the company, and they both receive the same remuneration of 10,000 PLN.

In accordance with legal regulations, Simon's remuneration cannot be his revenue expenditure but there are no obstacles to include Simon's remuneration in Gordon's revenue expenditure, and vice versa. As a result, the revenue of each partner will be reduced by the other partner's remuneration.

5) Expenses related to the use of a passenger car that is not entered in the fixed asset register in the part that exceeds the amount being the product of: the number of kilometres actually driven and the rate per kilometre driven.

A taxable person using a passenger car for business purposes where the car is not a fixed asset and is not used under lease, is required to keep the vehicle kilometre logbook. Keeping the logbook is a basic prerequisite if a taxable person wants to recognise car-related expenses as revenue expenditure.

Cars that are most frequently used for business purposes are the entrepreneurs' own cars, own cars of employees used for business travel, and cars used under rental or lending agreements, etc. Recognition of expenses related to the use of such cars under revenue expenditure is dependent on keeping the vehicle kilometre logbook (except for the situation where the employee accounts for the car use expenses in the lump-sum scheme).

In accordance with Article 23 para. 5 of the PIT Act, if no vehicle kilometre logbook is kept, a taxable person's expenses on the use of cars for their own purposes are not revenue expenditure.

The obligation to establish the logbook stems from the fact that a taxable person may not recognise under revenue expenditure all expenses related to the car which is not their own or leased asset, but only such portion of these expenses that is connected to the person's business activity. The amount of expenses which may be considered expenditure is limited to the product of: kilometres driven for business purposes and the rate per kilometre driven that is specified in the legal regulations.

A vehicle kilometre logbook is thus kept to establish the limit of expenses that may be recognised under revenue expenditure. In addition to a vehicle kilometre logbook, a taxable person should also keep a list of car-related expenses (fuel purchases, repairs, parts, fees).

6) Expenses incurred for the account of employees who use their own cars for the enterprise's purposes:

   a) in order to travel on business (long-distance travel) – at the amount exceeding the amount determined by applying the rates per kilometre driven;
   b) local travel – at the amount exceeding the amount of a monthly lump sum of money, or exceeding the rates per kilometre driven, as specified in separate regulations issued by a competent minister.

An employer is often obliged to reimburse the employee for expenses incurred in connection with the use of the employee's own car for business purposes. Recognition of the employer's expenses under expenditure faces the limitations referred to above.

An employee who uses their own car (or other car that is not owned by the employer) is required to keep a vehicle kilometre logbook, and only the expenses disclosed in the logbook may be tax expenditure.

Expenditure in excess of what is disclosed in a vehicle kilometre logbook will not be considered tax expenditure.

Summary

A general rule is that an expense may be considered revenue expenditure if it is related to revenue and is not excluded from revenue expenditure. The catalogue of exclusions is quite extensive though.

What is more, in some cases legal regulations are ambiguous, and as such may give rise to disputes with tax authorities. One should thoroughly read the catalogue of expenses that may not be considered expenditure, because any mistakes can be costly. And as we know, tax arrears and the interest on them we cannot include among tax expenditure either.

NON-RESIDENT TAXATION – WITHHOLDING TAX

A specific group of taxable persons are non-residents, i.e. people whose place of residence is not Poland, yet they earn their income here. Taxation applied to such income will be governed by double taxation conventions. In many situations, non-residents' income will be subject to taxation in the "source country", i.e. in the country where income is earned.

In the case of certain income, taxation of a non-resident in Poland does not differ from taxation of residents, i.e. persons whose place of residence is Poland. Hence, there are no special differences between residents and non-residents with regard to taxation of income from employment or a business activity.

On the other hand, some fundamental differences apply in the first place to income derived from contractual professional services (e.g. under civil law agreements or management contracts) or related to copyright or interest. Such revenue earned by non-residents is taxed with 20% lump-sum income tax.

Provisions relating to the lump-sum tax are applied taking into account double taxation conventions. In order to be able to apply a tax rate resulting from a relevant double taxation convention and thus not collect (not pay) the tax under such convention, a taxpayer must obtain a taxable person's tax certificate of residence.

Since no revenue expenditure is deducted from such revenue, the lump-sum tax is calculated on the revenue.

Non-residents who earn the said revenue without taxpayers' intermediation are obliged, with no prior notice, to pay the lump-sum income tax for the months in which such revenue was obtained, by the 20th day of the month for the preceding month.

If such revenue is earned with taxpayer's intermediation, it is the taxpayer that is obliged to calculate, collect and pay the due amount of the lump-sum tax. A taxpayer pays the tax by the 20th day of the month following the month in which the tax was transferred to the bank account of a tax office managed by the head competent for the taxpayer's domicile or registered office.

A taxpayer does not collect the lump-sum tax if a non-resident carries out a business activity in Poland through an establishment located here. However, for the tax not to be levied, a taxpayer must obtain from a taxable person a certificate confirming the existence of a foreign establishment in Poland issued by a competent tax authority of the state in which the taxable person is domiciled, or by a tax office in Poland competent for such establishment. In addition, the taxpayer must obtain a written statement from a taxable person that the dues concerned are related to the establishment's operation.

Taxpayers who discharge such performances for a person not residing in Poland are obliged to send to a taxable person concerned and a competent tax office, by the end of February following the tax year concerned, a personal notification of revenue (income) earned by individuals whose place of residence is not Poland (IFT-1R). If a taxpayer closes their business down before the end of February, they should prepare and send such notification for the relevant period and by the business closing date.

Following a foreign person's written request – within 14 days of its submission – a taxpayer is obliged to prepare IFT-1 notification and send it to the taxable person and a competent tax office. Submission of such notification does not relieve the taxpayer from the obligation of submitting the IFT-1R notification by the end of February.

The right to file an annual tax return by a foreigner whose lump-sum income tax was collected by a taxpayer

As we can infer from the above-described rules governing lump-sum personal income tax of non-residents, the PIT Act differentiates the tax treatment of income earned by persons residing and not residing in Poland.

Revenue that for non-residents is taxed at the lump-sum rate of 20%, for persons residing in Poland is taxed according to the taxable bands (18% and 32%).

What is more, the latter group is entitled to reduce their revenue with expenditure (usually at the lump-sum percentage of 20% or 50%).

As a result, Polish residents and non-residents pay different taxes on income from the same source.

Example:

A person residing in Poland earning gross revenue of 1000 PLN under a specific-task contract will pay tax of 144 PLN (18% of 800 PLN, i.e. revenue of 1000 PLN reduced by revenue expenditure of 20%, i.e. 200 PLN).

In contrast, a non-resident in Poland will pay for the same specific-task contract performed in Poland the tax of 200 PLN (20% of 1000 PLN).

This discrimination has been pointed out to Poland by the European Commission, which takes care that national laws in the Community do not contain regulations that may be considered discriminatory against citizens of other Member States of the EU. As a result, the discrimination was eliminated with effect from 1 January 2009. Now, each non-resident living in the EU or within the EEA has the right to recover the overpayment resulting from a taxpayer's withholding of the lump-sum income tax (which is usually higher than the tax calculated according to the taxable bands).

In order to recover the overpaid amount, a taxable person must file with a tax office an annual tax return with an attached tax certificate of residence from their country of residence. In their return, the taxable person will disclose their revenue earned in Poland, reduce it by the lump-sum expenditure that is provided for by legal regulations, and then apply to the resulting income a tax rate from a relevant taxable band. The lump-sum tax of 20% collected before will be thus treated by the taxable person as an advance tax, and so they will be able to recover the overpayment.

APPLICATION OF DOUBLE TAXATION CONVENTIONS BY RESIDENTS AND NON-RESIDENTS

Taxable persons earning income from abroad are faced with the obligation to tax such income correctly. In other words, they must apply the provisions of double taxation conventions.

What is double taxation? How can it be prevented, and what issues are governed by such conventions?

According to the income tax laws, taxable persons that have their place of residence or registered office in Poland are taxable in Poland on their entire income, including that earned abroad. However, such income may also be taxable in the country where it is earned. We deal with double taxation in a situation where two states levy the same or similar taxes on income or assets (capital) obtained under the same arrangements by the same taxable person in the same period.

Such phenomena are very harmful. That is why the interested states take measures that are designed to prevent their occurrence or at least mitigate their effects.

These measures are included in bilateral double taxation conventions. The rules contained in such conventions determine how to tax income or assets (capital) if a person having their place of residence or registered office in one state earns income in the other contracting state.

Pursuant to the Constitution of the Republic of Poland, international agreements become generally applicable sources of law once they are ratified and published in the Journal of Laws. Therefore, double taxation conventions concluded by Poland with more than 80 countries are applied directly in order to decide how to tax foreign income.

Double taxation conventions are usually formulated in accordance with the model developed by the Organisation for Economic Co-operation and Development (OECD). The model is known as the Model Tax Convention on Income and on Capital. Another widely accepted model of such conventions is the UN Model Double Taxation Convention between Developed and Developing Countries.

Both models have a similar structure and include similar definitions and methods for elimination of double taxation.

The interested states that intend to sign a double taxation convention are not obliged to use any of these models. As a rule, however, they do. The interested states are of course free to modify individual provisions included in the models.

Conventions entered by Poland are based on the provisions of the OECD Model Convention. The Model Convention is supplemented by the Commentary, which explains how the signatory states understand and interpret its stipulations.

Neither the OECD Model Convention nor the Commentary are the sources of law in Poland, but Poland – as a member country of the OECD – is obliged to apply the Convention and the Commentary, and the tax authorities should refer to the Commentary in both the application and interpretation of double taxation conventions in order to ensure a uniform application of the law.

Individual conventions based on the Convention are addressed to persons that have a place of residence or a registered office in one of the states, and relate to income and property taxes that are levied by both contracting states.

Double taxation conventions resolve how to tax the following categories of income and assets (capital):

- income from immovable property;
- business profits;
- profits from international transport;
- profits of associated enterprises;
- dividends;
- interest;

- royalties;
- profits from alienation of property;
- income from liberal professions;
- profits from dependent personal services;
- directors' fees and remunerations of supervisory board members;
- remuneration of artists and sportsmen;
- pensions;
- salaries of government service;
- income of students;
- other income.

In addition, individual conventions include provisions concerning methods for elimination of double taxation.

In the conventions entered by Poland, we can find two methods for elimination of double taxation:

exemption with progression and the principle of credit.

Double taxation conventions also include the provisions concerning equal treatment of citizens of both states by tax jurisdictions of such states, procedures for the exchange of information and mutual assistance of tax administrations, and specific provisions (if any).

In order to ensure a proper taxation of their foreign income, a taxable person should in the first place use a relevant convention to decide which state they are a resident of (in this state they will be subject to taxation on their entire income). Then, they should determine which taxation method is provided for by the convention in respect of their income. In a situation where the convention specifies that the income in question may be taxed both in the country of residence (registered office), and in the country where the income was earned (the source country), then to the taxation of such income in the country of residence one should use an appropriate method for elimination of double taxation. To the income which, in accordance with the convention, is subject to taxation in Poland, one should apply the provisions of Income Tax Acts.

The oldest and still effective double taxation conventions were signed by Poland back in the 1970s. For many years, the conventions have only applied to a handful of people. Poland's accession to the European Union and opening up of foreign labour markets have transformed the conventions into truly universal legal acts the knowledge and appropriate application of which becomes simply essential.

Rules for determining tax residence

Place of residence

Double taxation conventions do not contain own definitions of the place of residence.

According to the conventions, the term “resident of a contracting state” means any person who, under the laws of that state, is liable to tax therein by reason of his domicile, residence, place of management, place of incorporation, or any other criterion of a similar nature. So, if for example Polish regulations recognize that a person has a place of residence in Poland, then on the basis of a double taxation convention, the person will be considered to be a person who lives in Poland.

Determination of the place of residence should therefore start from reviewing Polish regulations that govern this issue.

Pursuant to Article 3 para. 1a of the Personal Income Tax Act:

"A person having their place of residence in the territory of the Republic of Poland is understood as an individual who:

1) has their centre of personal or economic interests (centre of vital interests) in the territory of the Republic of Poland, or
2) stays in the territory of the Republic of Poland for more than 183 days in a tax year".

Even if only one of these conditions is satisfied, it will mean that an individual will be considered a Polish resident in accordance with the Polish legal regulations.

The first of these conditions refers to the "centre of vital interests", which consists of a centre of personal or economic interests. The conjunction "or" in this provision means that it is sufficient to have at least one of such centres in Poland to be considered a person living in Poland.

Example:

John goes to work in the Netherlands. Ha rents a flat there, opens a bank account, and stays in the country for more than 183 days in a year. He even joins a trade union in his Dutch plant. He has no assets in Poland.

So one could say that he has moved the centre of his economic interests to the Netherlands. However, John's wife and children stay in Poland and live in his parents' house. Therefore, John's centre of personal interests is still in Poland.

Consequently, he will be subject to the unlimited tax obligation in Poland. When his family leaves Poland to join him in the Netherlands, it will be possible to conclude that John's centre of vital interests is located in the Netherlands.

John's transfer of his personal interests to another country will be primarily proven by the fact that he lives with his family in that country. Other personal relations, such as: friends, hobbies, cultural or other activities are certainly not as tight as family relations. The transfer of economic interests is testified in the first place by the fact that a taxable person earns most of (and preferably the entire) income in a new country.

The second condition contained in the regulation provides that a person has their place of residence in Poland if they stay in the country for more than 183 days in a tax year. We should note here that it does not have to be an uninterrupted stay. In order to determine whether a taxable person is subject to the unlimited tax obligation in Poland, we have to count the days of their stay in the country.

In real life, it often happens that two states recognise a taxable person as a resident of their territory.

Example:

A Czech is delegated by his employer to work in Poland for a year.

Once his stay in Poland exceeds 183 days in a given tax year, he will become a person having a place of residence in Poland.

Most likely, however, the Czech legislation will consider him a resident in the Czech Republic.

This situation is a "residence conflict" – that is a case where two states consider the taxable person is their resident. Pursuant to double taxation conventions, an individual may have a place of residence in one state only, and can be subject to the tax obligation on their entire income in one state only too. Therefore, any "residence conflict" should be resolved in line with the provisions of double taxation conventions.

Resolving the issue of the place of residence on the basis of double taxation conventions

If, within the meaning of the applicable provisions of both contracting states, a person has a place of residence in both states, then their place of residence is determined in line with the following principles, as set out in double taxation conventions:

a) a person shall be deemed to be a resident only of the contracting state in which he has a permanent home available to him; if he has a permanent home available to him in both contracting states, he shall be deemed to be a resident only of the state with which his personal and economic relations are closer (centre of vital interests);
b) if the state in which he has their centre of vital interests cannot be determined, or if he has not a permanent home available to him in either state, he shall be deemed to be a resident only of the state in which he has a habitual abode;
c) if he has a habitual abode in both contracting states or in neither of them, he shall be deemed to be a resident only of the state of which he is a national;
d) if he is a national of both contracting states or of neither of them, the competent authorities of the contracting states shall settle the question by mutual agreement.

The above criteria should be applied in the order specified above, that is, if one is unable to resolve a given issue according to a), one should move to b) and so on.

The first criterion that is used to resolve which country is a taxable person's place of residence is a permanent home. According to the Commentary to the OECD Model Convention, a permanent home is understood as a 'hearth and home', i.e. the place where a taxable person's family and personal life is concentrated. It does not matter whether a taxable person has a legal title to that place.

If a person has a permanent home in both contracting states (for example, they have two permanent homes and stay in each of them for part of the year), then the right of residence is granted to that country with which the personal and economic relations of the taxable person are closer, this being understood as the centre of vital interests. The concept of a centre of vital interests, which can be found in double taxation conventions, should be interpreted in the same way as it is interpreted pursuant to the PIT Act. It is therefore necessary to examine with which of the two countries the taxable person is bound with stronger personal and economic relations. A place of residence of the taxable person's immediate family (spouse, children) is of primary importance here.

Where a taxable person has no permanent home in any of the states concerned, and it is impossible to determine in which state they have a centre of vital interests (because they have personal and economic relations with both states), they shall be deemed a resident of the country in which they have a habitual abode.

By a "habitual abode" we mean staying in one state for longer than in the other one. If it cannot be resolved in which country a taxable person has a habitual abode (because they stay in both states or in neither of them), then the person shall be considered a resident of the country of which they are a national. Thus, citizenship is only a third-grade criterion in determining the place of residence.

If, however, this condition does not result in the final determination either (because a taxable person is a national of both states concerned or neither of them), then the taxable person's place of residence would have to be decided by the authorities of both states by mutual agreement.

In most cases, it is possible to determine the place of residence on the basis of the "centre of vital interests" criterion.

Registered office (permanent establishment)

According to the OECD Model Convention, the term "a person having their permanent establishment in a contracting state" means a person that, under the laws of that state is subject to the tax obligation in that state because it is their place of management or based on any other criterion of a similar nature.

If a person other than an individual has a permanent establishment in two contracting states, then it is believed that they are a resident of the contracting state in which it has a place of effective management.

The place of effective management is the place where key management and commercial decisions that are necessary for the conduct of the enterprise's business are made. The place of effective management will usually be the place where a person or group of persons holding the top functions (such as the board of directors) takes official decisions.

The Commentary to the OECD Model Convention recognizes that no exact standard can be specified on this subject, but all relevant facts and circumstances must be examined to determine the place of effective management.

An entity may have more than one place of management, but it can have only one place of effective management at any one time.

Tax certificate of residence

Pursuant to the above provisions, a taxable person's residence (i.e. the place of residence or registered office) is therefore determined by the facts rather than fulfilment or non-fulfilment of some formal requirements (for instance the mere fact of having the permanent registered address in Poland does not suffice to prove that the person has the place of residence in Poland).

However, in some cases, a taxable person may need an official confirmation of their residence. Then, at the taxable person's request, tax authorities issue a certificate stating the place of residence (registered office), known as a tax residence certificate.

According to the definition specified in the Income Tax Act, a tax certificate of residence is a certificate stating a taxable person's place of residence for tax purposes, issued by a competent tax authority in the taxable person's state of residence.

Issuance of a tax certificate of residence by the Polish tax authorities is regulated by Article 306l of the Tax Code, according to which a tax authority, at the request of a taxable person, issues a certificate stating their place of residence or registered office for tax purposes within the territory of the Republic of Poland.

Polish legislation does not indicate formal requirements to be met by a foreign tax certificate of residence, or state what information should be included in the certificate. However, a certificate should be a document issued by the tax authorities of the country concerned, confirming that the person has a place of residence in that country and is taxable on their entire income in that country.

It happens that Polish tax regulations require that income of non-residents should be taxed in a different way than provided for by a double taxation convention.

In such cases, it will be possible to apply the provisions of the convention and not of the act (e.g. by a taxpayer collecting a tax or tax advance), if a non-resident submits a tax residence certificate issued by the other state.

Taxation of selected sources of revenue in accordance with double taxation conventions

Dividends

According to the OECD Model Convention, dividends paid by a company which is a resident of a contracting state to a resident of the other contracting state may be taxed in that other state.

However, such dividends may also be taxed in the contracting state of which the company paying the dividends is a resident and according to the laws of that state, but if the beneficial owner of the dividends is a resident of the other contracting state, the tax so charged shall not exceed:

- 5% of the gross amount of the dividends if the beneficial owner is a company (other than a partnership) which holds directly at least 25% of the capital of the company paying the dividends;
- 15% of the gross amount of the dividends in all other cases.

So the regulations allow for taxation of dividends in both states. Double taxation is eliminated in such a way that a taxable person may deduct the tax paid in the source country from the tax due in the state of residence.

Royalties

Royalties arising in a contracting state and beneficially owned by a resident of the other contracting state shall be taxable only in that other state.

The term "royalties" means payments of any kind received as a consideration for the use of, or the right to use, any copyright of literary, artistic or scientific work including cinematograph films or tapes for the radio or TV, any patent, trade mark, design or model, plan, secret formula or process, as well as for the use of, or the right to use, industrial, commercial or scientific equipment, or for information concerning industrial, commercial or scientific experience.

Income from dependent personal services

In accordance with the provisions of double taxation conventions, salaries, wages and other similar remuneration derived by a person having their place of residence in Poland in respect of dependent personal services shall be taxable only in Poland, unless such independent personal services are rendered in the other state. If such services are so rendered, such remuneration may be taxed in that other state.

This principle means that remunerations are generally subject to the tax in the country where the services are rendered. Conventions also allow for taxation of labour income in the state of residence, but in this case, an appropriate method for elimination of double taxation should be employed.

Of course, every rule has an exception, and so has this one.

Remuneration derived by a resident of Poland in respect of dependent personal services rendered in the other state shall be taxable only in Poland, if all three conditions are satisfied:

a) the employee is present in the other state for a period or periods not exceeding in the aggregate 183 days in any 12-month period commencing or ending in the fiscal year concerned;
b) the remuneration is paid by, or on behalf of, an employer who is not a resident of the other state;
c) the remuneration is not borne by a permanent establishment which the employer has in the other state.

If the above conditions are satisfied, then the remuneration of an employee working abroad will still be taxable in Poland, so no double taxation will occur. If one or more of the above conditions is not met, the employee's remuneration will be taxable in the country in which they render services.

a) Remuneration will be subject to the tax abroad, if the period of work exceeds 183 days:

In most cases related to posting of employees to work abroad, the place of taxation for remunerations will be determined based on the employee's period of stay abroad.

Example:

Henry is employed at a Polish construction company. Starting from 1 April 2012, he is posted to work at a construction site in Estonia. During the period of secondment his remuneration is paid by the company in Poland. He comes back to Poland on 1 August 2012, and starting from 1 March 2013 he is posted again to Estonia where he works until 31 August 2013.

As a result, in the 12-month period between 1 April 2012 and 31 March 2013, his stay in Estonia was 153 days (i.e. it has not exceeded 183 days), but during the 12-month period calculated backwards from the date of return, i.e. from 31 August 2013 to 1 September 2012, his stay in Estonia was 184 days.

A double taxation convention signed with Estonia provides that a remuneration shall be taxable in Estonia, if an employee stays in Estonia for a period or periods exceeding in the aggregate 183 days in any 12-month period commencing or ending in a given tax year. Therefore, for the period of work between 1 March 2013 and 31 August 2013, the employee will be subject to the tax in Estonia.

The Commentary to the OECD Model Convention provides a simple method to determine the length of the employee's stay in the other country. So, in order to determine the number of days of stay in the other country, one should count "days of physical presence", as the employee is either present in a given country or not. We must therefore take into account the following elements: part of a day, day of arrival, day of departure, and all other days spent inside the state (weekends, holidays, days of sickness, etc.).

b) Remuneration is paid by, or on behalf of, an employer who is not a resident of the other state:

Remuneration of an employee posted to work abroad may be taxable in that country regardless of the employee's length of stay. Such a situation will occur where the employee's departure to work at a foreign counterparty will involve a change of the employer.

It should therefore be noted that since the term "employer" is not defined in the Convention, it is understood that the employer is a person having the right to conduct the work and bearing the associated risk and responsibility.

In case of international labour lease, these functions are largely performed by the user of the workforce. Therefore, when employees are leased, we may deal with the change of the employer within the meaning of double taxation conventions.

c) The remuneration is not borne by a permanent establishment which the employer has in the other state:

If a company has a foreign permanent establishment or a fixed place of business through which it conducts an important part of its business activity abroad, then the establishment becomes an entity that is subject to taxation in the country in which it is located. A permanent establishment may be a factory, an office, a branch or a construction site (provided that it exists for more than 12 months).

Since an establishment becomes the entity that is subject to taxation in a given country, in order to determine the establishment's income, we take into account the revenue that is generated by the establishment and the expenditure that is incurred by the establishment (or by the headquarters for the establishment's account). Thus, remunerations of employees working at the establishment will undoubtedly be the establishment's expenditure (even if the remuneration is paid by the headquarters and not the establishment).

At the same time, remunerations will be taxable in the state where the establishment is located. Of course, the mere fact of having an establishment in a given state does not mean that every employee who works in that state performs work for that establishment.

Example:

A Polish company has a factory in the Czech Republic, which produces sub-assemblies. Remunerations of employees employed in the factory are naturally subject to the tax in the Czech Republic. But the remuneration of an employee who have been seconded from Poland to a contractor in the Czech Republic for a period of 4 months in order to train local employees will be subject to taxation in Poland.

Remuneration of sailors

Remuneration in respect of an employment exercised aboard a ship or aircraft operated in international traffic, or aboard a boat engaged in inland waterways transport may be taxed in the state in which the place of effective management of the enterprise is situated.

Liberal professions (professional services) and other independent personal services

Pursuant to double taxation conventions, the term "liberal profession" ("professional services") includes especially independent scientific, literary, artistic, educational or teaching activities as well as the independent activities of physicians, lawyers, engineers, architects, dentists and accountants.

Income derived by a person having their place of residence in Poland form a liberal profession (professional services) or any other independent activities is taxable only in Poland, unless that person usually has a permanent establishment in the other country for the exercise of their activities. If they have such permanent establishment, then their income may be taxed in that country, but only to the extent to which it may be attributable to that permanent establishment.

Taxation of income of members of corporate decision-making bodies

Directors' fees and other similar payments derived by a resident of a contracting state receives in his capacity as member of the board of directors or supervisory board of a company which is a resident of the other contracting state may be taxed in that other state (Article 16 of the OECD Model Convention).

In accordance with the above regulation, income in respect of a supervisory or managerial function in a company having their registered office in a given state will be taxed in that state (the source country).

If a person, apart from holding an executive position, performs other services for the company, for example, on the basis of a contract of employment, and receives remuneration for such services, then the above-mentioned rules will apply to that portion of remuneration that is paid for the provision of supervisory or managerial services.

Rules governing taxation of enterprise income

Profits of an enterprise of a contracting state shall be taxable only in that state unless the enterprise carries on business in the other contracting state through a permanent establishment situated therein. If the enterprise carries on business as aforesaid, the profits that are attributable to the permanent establishment may be taxed in that other state.

As we have already said, a permanent establishment is a fixed place of business through which an enterprise conducts a business activity in the other state. If a company has a permanent establishment, one should determine (on the market basis) the amount of the establishment's profits and tax them in the country in which the permanent establishment is situated.

Methods for elimination of double taxation

Where a resident of Poland derives income which may be taxed abroad (such as income from employment in a foreign company), then we deal with double taxation: such income is taxable abroad, while the person who has earned it, is taxable in Poland. As I have already mentioned at the beginning of the lesson, double taxation is a very harmful phenomenon. That is why the interested states take measures that are designed to prevent its occurrence. These measures are included in bilateral double taxation conventions.

In double taxation conventions that have been concluded by Poland, we deal in principle with two methods for elimination of double taxation: exemption with progression and the principle of credit.

Exemption with the progression method

This method for elimination of double taxation is provided for in the majority of conventions concluded with European countries, including: Albania, Croatia, Cyprus, Czech Republic, Estonia, France, Germany, Greece, Italy, Latvia, Lithuania, Portugal, Romania, Slovakia, Slovenia, Sweden, Turkey and the UK.

If this method is used, it means that foreign income is tax-exempt in Poland.

However, in order to determine the tax rate on the remaining income – i.e. the income earned in Poland – one applies the tax rate that is appropriate for the entire income, i.e. including the income earned abroad.

Example:

Let us assume that a taxable person in 2012 earns income in Germany in the amount of 79,000 PLN (converted into PLN) and in Poland in the amount of 40,000 PLN (we do not take into account the social security (ZUS) and health contribution).

To the taxable income (i.e. that earned in Poland), we apply the percentage rate that would be applicable if the German income was not tax-exempt.

We calculate the rate as follows:

1. We calculate the tax on taxable and exempt income:

   40,000 PLN + 79,000 PLN = 119,000 PLN,

   (119,000 PLN – 85,528 PLN) x 32% + 14,839.02 PLN = 25,550.06 PLN;

2. We divide the tax by the sum total of income and multiply the result by 100:

   25,550.06 PLN / 119,000 PLN x 100 = 21.47%

   (we round the rate to two decimal places);

3. We apply the calculated percentage to the taxable income:

   40,000 PLN x 21.47% = 8588 PLN

   So the tax will be 8588 PLN.

Credit method principle

This method is provided for in conventions concluded, among others, with: Belgium, Kazakhstan, the Netherlands and Russia.

If this method is used, it means that foreign income is taxable in Poland, but the tax paid abroad is deducted from the tax due. However, this deduction must not exceed the amount of the tax chargeable in proportion to the income earned abroad.

Example:

Let us assume that a taxable person in 2012 earns the same income as in the previous example, except that in a different country: in the Netherlands in the amount of 79,000 PLN and in Poland in the amount of 40,000 PLN (we do not take into account the social security (ZUS) and health contribution). We assume that the tax paid abroad amounted to 7907 PLN.

So the total (Polish and Dutch) taxable income will be 119,000 PLN.

1. We calculate the tax on the total income:

   40,000 PLN + 79,000 PLN = 119,000 PLN,

   (119,000 PLN - 85,528 PLN) x 32% + 14,839.02 PLN = 25,550.06 PLN;

2. We deduct the tax paid abroad from the tax. However, this deduction must not exceed that part of the tax that is chargeable in proportion to the income earned in the Netherlands. Income earned in the Netherlands (79,000 PLN) represents 66.39% of the taxable income, so we can deduct a maximum amount of:

   25,550.06 PLN x 66.39% = 16,962.68 PLN;

3. Since the tax paid in the Netherlands amounted to 7907 PLN, we can deduct it in full:

   25,550.06 PLN – 7907 PLN = 17,643.06 PLN.

   Consequently, the tax due in Poland (rounded off to the nearest whole zloty) amounts to 17,643 PLN.

Summary

Double taxation conventions are aimed at resolving issues that may arise in the case of overlap of tax regulations of two states. The fact that income is earned abroad does not mean that it will not attract the attention of the Polish tax authorities, yet owing to a relevant double taxation convention we will not have to pay the tax twice on the same income.

VAT

Where does the name VAT come from? It is the English abbreviation of "Value Added Tax". In Polish literature and everyday language, it is also commonly referred to as tax on goods and services, and abbreviated to PTU.

Contrary to popular belief, a similar tax can be found not only in the European Community; it is quite common worldwide (for example, in Canada, Australia and New Zealand the tax is known as GST – Goods and Services Tax). The difference in the basic rates of the tax in individual countries is very large, and it is the basic rate that actually determines the tax importance in shaping the tax and price environment of the country.

VAT and tax authorities

VAT is the apple of the tax authorities' eye. It comes as no surprise since VAT and excise duty are the main sources of income for the state budget. In addition, VAT is extremely vulnerable to abuse (we will explain why in a little while). Hence, we are confronted with dozens of safeguarding and detailing provisions; therefore we have to deal with VAT refund and deduction problems. Finally, the special attention of tax officials inspecting the tax settlements, as well as special requirements for VAT-related documents, record-keeping obligations, etc.

Given all these factors, VAT seems a difficult tax to settle.

What is VAT really?

VAT is an indirect tax, added to the price by active VAT payers (i.e. such taxable persons that are obliged to increase the price of their goods and services by the tax) every time there is a supply of goods or services, except when the supply is tax-exempt or taxed at a preferential rate of 0%. However, each active taxable person making taxable sales has the right to deduct from the tax added to the price at the sales transaction (in settlements with tax offices and in the legal regulations referred to as the output tax) the tax that has been charged by other active VAT payer on supplies of goods and services needed to make taxable sales.

Example:

Let us take a look at an entrepreneur that is an active VAT payer and is engaged in the business of selling industrial goods. Such types of sale are subject to VAT at the applicable tax rate (currently 23%).

It is clear that in order to sell a product, one must first purchase it.

While purchasing goods and services, VAT payers use the concepts of the net and gross price. The net price is VAT exclusive, whereas the gross price is the one with the tax. Because the tax is usually included in the price of purchased goods or services, entrepreneurs will be able to deduct the tax at a later stage of the cycle. Therefore, they pay attention mainly to the net price. That is what differentiates them from ordinary consumers, who will not be able to deduct the VAT paid in the price, and who thus focus on the gross price.

So an entrepreneur buys commercial goods from a wholesaler. A total of 100,000 PLN net is spent on these goods. This means that they have to pay to the suppliers 123,000 PLN gross (100,000 PLN + 23% VAT).

They then sell the same goods to consumers or other entrepreneurs, but this time the price is 140,000 PLN net. This means that they have to increase the price by 23% VAT (23% on 140,000 PLN, i.e. 32,200 PLN).

If entrepreneurs could not deduct the VAT that has been charged at previous stages in the cycle, than the entrepreneur from the example would have to pay to the state budget the full amount of VAT that they have collected from purchasers of their goods (that's right! – while collecting the price for the goods, any entrepreneur that is an active VAT payer becomes essentially a tax collector – which implies, of course, certain duties and responsibilities).

Fortunately, things are different here because the tax is collected on the added value. In our example, this added value is 40,000 PLN (goods are purchased for 100,000 PLN and sold for 140,000 PLN).

Let us see how the system works in its simplest form.

Upon the purchase of goods, the entrepreneur pays 23,000 PLN VAT (this amount has been added to the net price of the goods purchased). Upon the sales, they collect from customers as much as 32,200 PLN VAT.

Since the input tax (i.e. 23,000 PLN) can be deducted from the output tax (32,200 PLN), the entrepreneur will have to pay 9200 PLN tax (i.e. the difference between the output and input tax: 32,200 PLN – 23,000 PLN).

Please note: This amount is nothing but 23% on 40,000 PLN, i.e. the amount which constitutes the added value of the goods concerned. And hence the name: the value added tax.

At this point, it would be good to reflect on one issue: who actually pays the tax?

Although it is true that the entrepreneur from the example acts as the tax collector (receives the tax from the customer) and the tax payer – as they pay the tax in the amount due to a tax office, in fact the tax is paid by the consumer.

Of course the above example discusses a perfect, model situation. In the economic reality, taxable persons are unfortunately faced with limitations in deducting the input VAT on purchases, the necessity to limit the amounts deducted (on various grounds), or with the inability to recover the input VAT for a long time, etc.

But in essence it is the consumer who pays VAT to the state budget (with the consumer understood as the person who buys goods for consumption, i.e. for purposes unrelated to business activities).

Remember!

Your supplier is also an active VAT payer, and so they will perform a parallel tax calculation on their amount of added value. In this way, every participant in the trading chain adds the tax to the selling price and – while calculating the tax to be paid to a tax office – subtracts the tax that they themselves had to pay as part of the price of goods (services) purchased.

If so easy, why so difficult?

The above example might suggest that there is nothing easier in the world than VAT and its application.

After all, the rules for its calculation are trivial. So what makes the application of VAT so cumbersome, burdened with many document-related obligations, and why, in real life, will every taxable person sooner or later be faced with some VAT problems?

Things could be so simple. It would be enough to introduce one tax rate on all goods and services, without exemptions, exclusions, reliefs, exceptions or exempt entities. This, however, is impossible, from both social and economic reasons. We are also bound by the provisions of international law. In fact, Polish VAT regulations simply implement EU laws (although Poland still has some problems with VAT-related harmonisation). It all makes things more complicated.

The existing exemptions and differences in tax rates, as well as numerous limitations associated with tax deductions, and the need to settle transactions between entities that are located in different countries, mean the simple rules from the above-described example very rarely met in real life.

I would like to present here another example that shows how things can get complicated in a relatively simple situation.

This time our entrepreneur is a manufacturer of medical equipment, with individual items taxable at different rates. Depending on their intended use, individual components may be taxed at 0%, 8% or 23% (unfortunately, when the legislator decides to introduce reduced rates, the situation became complicated because there should always be someone who has to pay the basic rate, and care should be taken that that someone does not benefit from the reduced rate; besides, there are many other things to look after that we will discuss in a little while).

In order to be able to manufacture, an entrepreneur buys all kinds of materials, auxiliary materials, machinery, services, etc. Let us assume, for simplicity reasons, that while buying all the above items, they pay to the suppliers the net price plus 23% VAT.

So three situations may occur now (this is only an example; in real life, combined scenarios will also apply).

I. An entrepreneur buys goods and services for 100,000 PLN net, paying 23,000 PLN (23%) VAT at the purchase. This amount may be deducted from the output tax (in each scenario). They produce equipment and sell it for 140,000 PLN net, with the tax rate of 0%.
II. As above, but they sell the equipment for 140,000 PLN net, with the tax rate of 8%.
III. As above, but they sell the equipment for 140,000 PLN net, with the tax rate of 23%.

In the first scenario, the output tax is 0% on 140,000 PLN, i.e. 0 PLN. In the second scenario, the output tax is 8% on 140,000 PLN, i.e. 11,200 PLN. And in the third scenario, the output tax is 23% on 140,000 PLN, i.e. 32,200 PLN.

In each scenario, the entrepreneur has the right to reduce the output tax with the input tax paid at purchase, i.e. 23,000 PLN. And here starts the problem.

Let us analyse individual scenarios:

In examples I and II, the manufacturer is entitled to receive the tax REFUND from the tax office, but in scenario III, they have to pay the tax. You are not surprised then, that it is only natural that manufacturers often want to sell at the rate of 0% and get the refund from the tax office?

You are probably not.

But you should not be surprised either that tax authorities do everything in their power to ensure that the rate is applied solely and exclusively to the extent for which it is intended. And because we cannot have a tax official in every company, we have to deal with a multitude of regulations, records, returns, and – unfortunately – audits.

It would be much easier if sales of medical equipment in the example were taxed at a single rate only. But then social (and political) goals would not be pursued and achieved, and taxes are also, unfortunately, part of social policy.

Abuses

In the above example, we have dealt with an entrepreneur that is able to obtain an obvious tax benefit by applying different tax interpretations. If they do it in line with the applicable legal regulations, it is rational, honest and permitted conduct. However, the VAT application mechanism is such that it makes the tax very sensitive to fraud: one can create an artificial situation where the input tax is higher than the output tax, so the tax office will be required to refund the difference. Unfortunately, this is a common practice when groups of businesses are established whose sole purpose is VAT fraud.

Let us have a look at the following Example:

Company A (a fake enterprise registered only for fraud purposes) sells goods at the rate of 23% to Company B (another fake enterprise). Such sales are usually fictitious, but a method that fraudsters also employ is the massive inflation of the price (transactions between companies do occur, but their value is disproportionately high in relation to the actual market value).

Company B sells goods abroad (again fictitiously, to another bogus entity – Company C), applying the VAT rate of 0%. Since the sale is taxed at 0%, Company B is entitled to reduce the tax with the amount of VAT that is shown on the invoice received from Company A. Therefore, we have the input tax, but no output tax (0%).

So Company B applies to a tax office for a refund, and once it receives one, it vanishes into thin air.

Company A disappears as well without paying the output tax shown on the invoice.

Of course, Company C is equally difficult to track down.

Obviously, this example includes simplifications. There are numerous safeguards provided for in the legal regulations against such fraud (extending the refund period to allow the conduct of audit proceedings, a requirement to possess evidence of exports and supply, etc.). But if the system is so complicated, it is equally hard to tighten it up. If tax officials come across a gang of well-organised and determined fraudsters, fraud will happen.

The problem is that the tax authorities tend to generalize, and often treat honest taxable persons as cheaters. What is even worse, the legislator follows the same path by introducing new safeguards, reservations, and powers of auditing bodies to the existing regulations, thereby effectively complicating the already confusing system of VAT collection and calculation.

Definitions to remember

- output tax – tax that you add to the net price of goods or services that you sell;
- input tax – tax that your supplier adds to the net price;
- tax to pay – positive difference between the output and input tax;
- tax for refund – negative difference between the output and input tax.

International nature of VAT

As a Member State of the European Union, Poland is obliged to apply the EU regulations on VAT. This is because the tax is subject to the EU harmonisation: all states involved in trade are obliged to apply the same rules for calculations, refunds, limitations in deduction, rates, etc. This does not mean that the rates and rules are identical everywhere – harmonisation only applies to general issues.

A typical example of a general rule that is valid in the Union is that an active VAT payer is entitled to deduct the tax paid in connection with the purchase of goods and services related to taxable sales. This general principle has actually led the Polish state to several spectacular failures in the European Court of Justice. This is because the Polish legislator is often inclined to restrict the availability of tax refunds and deductions. Here the EU legislation is of help for taxable persons.

The essential EU act that Polish VAT payers should read is Council Directive 2006/112/EC. As with any directive, here we also deal with numerous implementing acts, which provide a detailed guidance for its application.

The national act that regulates VAT issues is the Act on Tax on Goods and Services dated 11 March 2004. Based on the powers delegated by the Act, the Minister of Finance (sometimes in consultation with another minister) issues a number of regulations that lay out the detailed conditions for the application of the Act.

VAT payers

The fact that a company or a person is a VAT payer does not automatically mean that they will add the tax to goods or services sold, or benefit from the deduction of the input tax related to purchases. This is because numerous exemptions, exceptions and exclusions apply to tax on goods and services.

In our discussion, we will focus on taxable persons that are engaged in business and business-like activities. We should remember, however, that in some unique situations, an individual who does not pursue a business activity may become a VAT payer as well. Individuals can be VAT payers, even if they are unaware of the fact, also in a situation where their activities will make them subject to the same treatment as is applied to persons engaged in a business activity.

It is the Act that determines whether we are VAT payers or not. The Act says that taxable persons under VAT include legal persons, non-corporate bodies and individuals that pursue an independent business activity, whatever the purpose or result of such activity.

And in the Act business activities are quite broadly defined. Hence, they include:

all activities of producers, traders or service providers, including entities extracting natural resources, and farmers, as well as persons in liberal professions, even if a single activity has been performed but in circumstances indicating an intention that it will be repeated.

A business activity also includes activities involving the use of goods or intangible assets on a continuous basis for commercial purposes.

This definition was changed on 1 April 2013. Since then, a business activity should be understood as all activities of producers, traders or service providers, including entities extracting natural resources, and farmers, as well as persons in liberal professions. A business activity includes in particular activities involving the use of goods or intangible assets on a continuous basis for commercial purposes.

Typical VAT payers include, for example, corporations and partnerships covered by the provisions of commercial and civil law, cooperatives and self-employed individuals, as well as persons who do not pursue a registered business activity but who are involved in repeated sales transactions of land or premises, or earning revenue from rent.

However, certain categories of activities are excluded from the statutory definition of a business activity. And so, the following are not considered to be independent business activities:

1) those activities the revenue from which is listed in Article 12 para. 1-6 of the Personal Income Tax Act – i.e. the activities performed as part of the service relationship, employment relationship, cooperative employment relationship and putting-out system;
2) those activities the revenue from which is listed in Article 13 item 2-9 of the Personal Income Tax Act, if due to performance of such activities, the persons concerned become connected with an entity commissioning the activities by a legal relationship which governs the conditions of performance, remuneration, and a liability of the commissioning entity towards third parties.

To express this rather complicated provision in simpler terms: if the results of a person's gainful activity constitute the responsibility of an employing entity (hirer, principal), then the activity is not a business activity.

Here is an *Example:*

An artist hires himself to perform a cabaret show. An organizer sells tickets; however, the artist cannot appear on stage for some reason. In this situation, it is the organiser that returns the ticket money and pays for the reserved venue. The organiser carries out such activities as part of their business.

We can also imagine a situation where an artist organises their performance on their own: they rent a venue, make promotional arrangements, hire a person to sells tickets, etc. Now, if the performance is cancelled, it is the artist who bears the financial consequences. If the said artist is repeatedly engaged in such activities, it will be considered that they pursue a business activity, even if it has not been registered.

So there is nothing left for us but to list the above-mentioned revenue that is specified in the Personal Income Tax Act in Article 13 item 2-9. So, the relevant revenue includes:

> Article 13
>
> (...)
>
> 2) revenue from contractual professional services: artistic, literary, scientific, coaching, educational and journalistic, including from participation in competitions in the field of science, culture and art, and journalism, as well as revenue from sports, sports scholarships awarded on the basis of separate regulations, and revenue of umpires/judges/referees related to sports competitions;
>
> 3) revenue of the clergy, other than that earned under a contract of employment;
>
> 4) revenue of Polish arbitrators participating in arbitration proceedings with foreign partners;
>
> 5) revenue earned by persons performing activities related to social or civic duties, regardless of how they are appointed, including compensation for loss of earnings, with the exception of revenue referred to in item 7;

6) revenue of persons to whom a state or local government authority or administrative authority commissioned, pursuant to relevant regulations, certain specific activities, especially revenue of experts in court, investigation and administrative proceedings, and payers, subject to Article 14 para. 2, item 10, and collectors of public debt, as well as revenue from participation in committees established by a state or local government authority or administrative authority, with the exception of revenue referred to in item 9;

7) revenue earned by persons, regardless of how they are appointed, sitting on management boards, supervisory boards, committees or other decision-making bodies of legal persons;

8) revenue relative to performance of services under a contract of mandate or a specific-task contract, derived exclusively from:

a self-employed individual, a legal person and its organisational unit, and a non-corporate body;

b) an owner (holder) of the real property in which premises are rented out, or a manager or administrator acting on behalf of such owner (holder) – if a taxable person renders such services exclusively for the purposes related to that real property

- with the exception of revenue earned under contracts concluded as part of the taxable person's non-agricultural business activities, and revenue referred to in item 9;

revenue earned under enterprise management contracts, management contracts or contracts of a similar nature, including revenue from these types of contracts concluded as part of a taxable person's non-agricultural business activities – with the exception of revenue referred to in item 7.

Doubts

In practice, interpretation of the provisions related to the scope of activities that are not an independent business activity has proved problematic. Let us have a look at two typical cases in which taxable persons were in doubt whether they were VAT payers or not:

A. A VAT payer carries out a business activity and at the same time earns revenue under specific-task contracts (contracts of mandate) whose subject matter goes beyond the scope of their business activities.

This is a situation dealt with in the above-cited Article 13 item 8 of the Act. If a contract provides that it is a principal that is fully liable towards third parties for the consequences of any irregularities in the execution of the contract, then there is no reason to treat such activities as performed by a VAT taxpayer. A typical example will be the situation where a taxable person runs a shop but also renders commissioned services (such as painting, translations/interpreting, artistic performances at parties, etc.).

B. A VAT payer carries out a business activity and at the same time earns revenue under specific-task contracts whose subject matter falls within the scope of their business activities.

The provision of Article 13 item 8 that we have just referred to excludes revenue earned under contracts concluded as part of a person's business activity any revenue related to the provision of services under a specific-task contract or a contract of mandate. Therefore, in this case, revenue from specific-task contracts will be subject to VAT.

Active and exempt VAT payers

The mere fact that someone has become a VAT payer does not mean that they will be required to add VAT to the price of their goods or services. This is because of the fact that one may be either an active VAT payer (where the taxable person enjoys full rights and is subject to all obligations under VAT regulations) or a VAT-exempt entity.

A taxable person that is VAT-exempt is relieved from the obligations of an active VAT payer, but cannot enjoy the rights vested in the latter either (e.g. deduct the input tax relative to purchases).

Taxable persons exempt based on the sales revenue criterion

The most common type of VAT exemption for persons engaged in a business activity is related to the turnover. So VAT exemption will apply to taxable persons whose taxable sales in a tax year do not exceed the total of 150,000 PLN. While determining the limit, we exclude the tax amount from sales (understood as the tax that would apply if a seller was an active VAT payer).

The limit value is also exclusive of supplies of goods and the provision of services that are tax-exempt, as well as goods that a taxable person classifies, pursuant to the income tax regulations, under fixed and intangible assets that are subject to depreciation/amortisation.

This exemption also applies to persons that start a business in the middle of the year. Later we will discuss the conditions for the use of such exemptions.

Record-keeping obligation of VAT-exempt taxable persons

If a taxable person wants to benefit from the exemption concerning tax on goods and services, they are obliged to keep VAT records so that they can identify the moment when they exceed the amount of revenue and thus lose the right to VAT exemption.

These records should be completed daily (EOD) but not later than prior to any sale transaction on the following day. If an entrepreneur keeps the tax book of revenue and expenditure, they may – instead of keeping the VAT records – use their sales records, which are kept in accordance with the Regulation on Keeping the Tax Book of Revenue and Expenditure, and in separate column there (usually column 15) disclose revenue that is subject to VAT and the total amount of their daily sales as resulting from invoices. In this case too, the entries must not be made later than prior to the first sale transaction on the following day.

Failure to keep the records may cost a taxable person dearly, if disclosed by a tax audit. If it is determined that an entrepreneur does not keep these records, or the records prove unreliable, the head of a tax office or a tax inspection authority will determine the non-recorded sales by estimate and levy a tax at 23%, excluding the right to reduce the output tax with the input tax paid at the purchase of goods.

Determining the exemption limit for taxable persons starting their business mid-year

Entrepreneurs often make a mistake assuming that that the limit of sales is a fixed figure for a given year, regardless of when they start their business. Meanwhile, if an entrepreneur takes up business activities that are subject to VAT in the middle of a tax year, they will be exempt from VAT if their expected sales do not exceed the limit amount in proportion to the duration of the sales period.

Of course, the question arises of how to calculate the ratio.

The amount at which the right to exemption will be lost is calculated using the formula:

elA = bA * D / 365

where:

elA – the amount which, if exceeded, will result in the loss of exemption;

bA – the bound amount, fixed for a given year;

D – the number of days remaining until the end of the year.

Resignation from exemption

Although it is applied by default, the turnover-based exemption is not obligatory.

On the contrary, a taxable person may resign from the exemption, provided that they submit a written notice to this effect to the head of a tax office, prior to the start of the month in which the waiver is to become effective.

Entrepreneurs who want to resign from the turnover-based exemption right from the start of their business should submit a relevant notice to the head of the tax office prior to the day when they complete the first taxable transaction.

Moment of the tax-exemption loss

Any taxable person using the turnover-based exemption should remain vigilant because the exemption ceases to apply if the limit amount is exceeded – that is when the tax obligation arises. The tax applies to the entire surplus of sales over the limit amount.

There are no transition periods here (such as: 'the tax will apply from the beginning of the day following the day when the limit has been exceeded).

Basic rights and obligations of VAT payers

As usually happens with taxes, the obligations considerably outweigh the3 rights. The primary right vested in active VAT payers is the possibility to deduct the tax paid on purchases related to taxable sales (unfortunately, if the payer's sales activities are VAT-exempt, the input tax on purchases will not be deductible – with a few exceptions).

An active VAT payer has the right to issue VAT invoices (but this is obviously an obligation too).

A taxable person is also entitled to the refund of VAT that they have not deducted from the output tax.

And what are the basic obligations of an active VAT payer?

They must issue VAT invoices and keep the records of VAT sales and purchases that are necessary for the correct preparation of tax returns. A taxable person is also required to prepare and submit to the tax office regular VAT returns. Last but not least, they must pay the amount of VAT payable, on the dates specified in the regulations.

TAX ON CIVIL LAW TRANSACTIONS

Tax on civil law transactions (TCLT) is a commonly paid tribute. Although VAT payers are often exempt from TCLT, there are numerous situations in which an entrepreneur will have to pay it.

Tax on civil law transactions is levied on:

1) the following civil law transactions:

    a) **contracts of sale and contracts of exchange of things and property rights;**
    b) **borrowing agreements concerning money or things specified only by type;**
    c) contracts of donation – in part concerning taking over by a donee of debts and burdens or obligations of a donor;
    d) contracts of annuity;
    e) contracts of distribution of estate and contracts of cancellation of joint ownership – in part related to payments or additional payments;
    f) establishment of a mortgage;
    g) **establishment of the usufruct for consideration, including irregular usufruct, and paid easement;**
    h) contracts of irregular deposit;
    i) **deeds of association;**

2) **amendments to contracts, agreements and deeds** referred to in section 1, if they result in an increase of the taxable base in tax on civil law transactions;
3) adjudications of courts, including courts of arbitration and court settlements, if they bear the same legal effects as civil law transactions referred to in section 1 or 2.

Entrepreneurs keeping a tax book of revenue and expenditure will usually have to deal with the transactions listed in items a, b, g and j, as these are common within the framework of economic relations.

However, within the framework of professional relations, the transactions referred to in item a, b and g occur most frequently between active VAT payers, or taxable persons that benefit from VAT exemption based on the turnover criterion. That is why a very important provision in the TCLT Act is the one that excludes the following entities from the operation of the Act:

- civil law transactions **other than a deed of association and its amendments, if at least one of the parties is subject to the following in respect of that transaction:**

a) is subject to tax on goods and services,
b) is exempt from tax on goods and services, except for:

- contracts of sale and exchange whose subject is real property or its part, or the right of perpetual usufruct, cooperative ownership right to premises, the right to a single-family house in a housing cooperative, or the right to a parking space in a multi-user garage, or interest in such rights;
- contracts of sale of shares and stock in commercial companies.
- The majority of transactions performed by entrepreneurs are thus excluded from the provisions of the TCLT Act.

Here are some examples

Adam buys commercial goods from a wholesale outlet. Because a wholesale outlet is a VAT payer due to its selling activity, the transaction is not subject to TCLT.

Henry borrows a certain amount of money from a limited liability company in which he holds interest. Since the company is a VAT payer in this transaction, it is not subject to TCLT; it does not matter here that the borrowings are statutorily exempt from VAT.

Ann leases a freezer from a company engaged in the supply of frozen food, for a fixed contractual amount. Because the company that owns the freezer is a VAT payer in the transaction, the contract will not be subject to TCLT.

And one more important exemption: TCLT-exempt are those transactions of **sale of movable property**, if the taxable base **does not exceed 1000 PLN.**

Determination of the taxable base

What is particularly important for the accuracy of tax settlements is the determination of the taxable base. The TCLT Act defines how the taxable base should be determined for each transaction subject to the tax.

Contract of sale

For a contract of sale, the taxable base is the market value of an item or a property right, which should be determined based on the average prices used in: trading in items of the same kind and type, taking into account their location, condition and wear, or trading in property rights of the same kind, **as applicable on the transaction day,** without deducting debts and burdens.

Indeed, disputes between taxable persons and tax authorities in the TCLT area are very often related to the determination of the taxable base. Many taxable persons were faced with the situation where a tax office considered that a car value stated in a car purchase agreement was understated compared to the market value. The TCLT Act provides for a special procedure to be followed in such situations.

If a taxable person fails to specify the value of an object in a civil law transaction, or the value specified by them does not correspond, in the opinion of a tax authority, to its market value, then the authority urges the taxable person to determine, increase or decrease such value. In a relevant notice, the tax authority will determine the time limit for fulfilling the request: it cannot be shorter than 14 days from the date when the notice was served. At the same time, the tax authority will give the proposed valuation of the transaction, as determined based on its own, preliminary assessment.

Here we have two alternatives to choose from: either to agree with the value specified by a tax official, or not. In the latter case, the tax authority will determine the market value taking into account an expert opinion **or an appraiser's valuation submitted by the taxable person**. If the tax authority appoints an expert, and the value determined based on their opinion differs by more than 33% from the value stipulated by the taxable person, then the latter bears the cost of opinion.

Contract of exchange

For a contract of exchange, the taxable base is:

a) in the case of residential premises constituting a separate property item or a cooperative ownership right to residential premises concerning the premises or the right to it – the difference between market values of the exchanged premises or rights to the premises;

b) in other cases – market value of a thing or a property right on which a higher tax applies;

Deeds of association

The taxable base is:

a) for conclusion of a deed – value of contributions to a partnership, or value of the share capital;
b) for payment or increase of contributions to a partnership, or an increase in the share capital - value of contributions that increase the partnership's assets, or the value by which the share capital has increased;
c) for capital injections – the amount of capital injections;
d) for a borrowing granted to a partnership/company by a partner/shareholder – the amount or value of the borrowing;
e) for transfer of things or property rights to a partnership/company for a free-of-charge use – the annual value of free use, which shall equal 4% of the market value of the thing or property right that has been transferred for a free-of-charge use;
f) upon business transformations or combinations – value of contributions to a partnership resulting from the transformation, or value of the share capital of a corporation resulting from the transformation or combination.

Other transactions

For a contract of donation, the taxable base is the value of debts and burdens or obligations taken over by a donee; upon establishment of the usufruct for consideration, including irregular usufruct, and paid easement – value of performances of a user or a person for which/whom the easement was established, for the period for which the rights have been established; and for a borrowing agreement and a contract of irregular deposit – the amount or value of the borrowing or deposit.

Amount of TCLT

Percentage rates of the tax are specified in the TCLT Act. In case of transactions that are most commonly performed by entrepreneurs, the applicable rates are:

1) on a contract of sale:
   a) of real property, movable property, right of perpetual usufruct, cooperative ownership right to residential premises, cooperative right to commercial premises, and the following pursuant to the cooperative law: the right to a single-family house and the right to premises in a small residential house **2%**;
   b) other property rights – **1%**;
2) on contracts of exchange, contracts of annuity, contracts of distribution of estate, contracts of cancellation of joint ownership, and contracts of donation:
   a) upon transfer of title to real property, movable property, right of perpetual usufruct, cooperative ownership right to residential premises, cooperative right to commercial premises, and the following pursuant to the cooperative law: the right to a single-family house and the right to premises in a small residential house **2%**;
   b) transfer of title to other property rights **- 1%**;
3) on a contract of establishment of usufruct for consideration, including irregular usufruct, and paid easement - **1%**;
4) on a borrowing agreement and a contract of irregular deposit – **2%**;
   a) on establishment of a mortgage:
   b) to secure an existing debt - on the amount of secured debt – **0.1%**;
5) to secure a debt of unknown amount – **19 PLN**;
6) on a deed of association – **0.5 %**.

Who has to pay the tax?

A civil law transaction usually involves two or more parties. It is therefore necessary to determine who is responsible for payment of the tax (the party obliged must be the one to record the tax in their tax book of revenue and expenditure). The Act resolves this problem.

The tax obligation is imposed on:

1) for a contract of sale – **on the buyer**;
2) for a contract of exchange – on parties to the transaction;
3) for a contract of donation – on the donee;
4) upon establishment of the usufruct for consideration, including irregular usufruct, and paid easement - **on the user or party acquiring the easement**;
5) for a borrowing agreement and a contract of irregular deposit – **on the borrower** or keeper;
6) in a deed of a civil partnership – **on partners**, and in other deeds of association – **on the partnership/company**.

Now it is time to deal with some specific situations that will appear in an entrepreneurs' daily business. Beware: The TCLT Act provides for many exemptions, exclusions, exceptions and deviations from these rules, so it is worth taking your time and reading it carefully at length. It is because I have only discussed here some frequent and typical situations.

Purchase of movable property from individuals who are not engaged in a business activity

If we are engaged in a business activity, we often buy all sorts of things from individuals who are not entrepreneurs. Because an exemption does not apply in respect of the VAT obligation on the side of the seller, and the buyer's (entrepreneur's) obligation will usually not arise at all (except in some specific cases set out in the VAT Act), the buyer (entrepreneur) will have to determine the value of the transaction and pay the relevant amount of TCLT. However, if the taxable base for the transaction does not exceed 1000 PLN, the transaction is tax-exempt. However, what if we buy from one person on the same day different things whose unit value does not exceed 1000 PLN, but the aggregate value actually does?

Please pay attention to the following provision of the TCLT Act: the tax applies to **contracts of sale**. So we can conclude that in order to determine whether a tax obligation arises or not, we should check whether a single contract exceeds the threshold. Therefore, if we conclude several separate purchase transactions, we must take into account the value of each contract separately in order to determine whether TCLT is payable.

Example:

1. We buy four chests of drawers at an online auction with the intent to resell. Each cost 500 PLN, but the purchase was made in a single auction. So we have concluded one contract only, and thus we will have to pay the tax of 40 PLN (2% on 2000 PLN).

2. We buy the same four chests of drawers for 500 PLN, but this time each of them was auctioned off separately. So we have concluded 4 contracts, each worth 500 PLN. Consequently, no TCLT obligation will arise.

Does this mean that if we buy several things at a flea market from the same person and at the same time with an intent to resell, we should consider likewise that we have concluded several contracts? In our opinion, yes - in this particular situation, each thing has been negotiated separately and we could modify terms of the contract for each thing (for example, as regards the time to return, warranty period, etc.). Beware: the Tax Code defines situations in which a tax authority may consider that taxable persons' activities were only meant to circumvent law (apparent legal acts were performed to minimise the taxable base). In the event of such a dispute, a taxable person will have to demonstrate that they have entered into separate contracts.

REAL PROPERTY TAX

Regulations concerning real property tax are included in the **Act of 12 January 1991 on Local Taxes and Charges** (consolidated text: J. of Laws of 1 June 2010, No. 95, as amended).

What is and is not subject to the tax?

Real property tax is levied on:

1) land;
2) buildings or their parts;
3) structures or their parts linked to running a business activity.

Real property tax does not apply to agricultural land, wooded land and scrubland within agricultural land or woods, **with the exception of land occupied for business purposes**.

Among other exemptions from real property tax, we should mention land under flowing surface waters and navigable channels, with the exception of lakes and land occupied by storage reservoirs or hydro-electric power stations. Other exclusions occur very rarely.

Taxable persons in real property tax

Taxable persons in real property tax are individuals, legal persons, non-corporate bodies and companies without legal personality, being:

1) owners of real property or civil structures;
2) owner-like possessors of real property or civil structures (if the object of taxation is held under independent possession, the real property tax obligation is imposed on the owner-like possessor);
3) perpetual usufructaries of land;
4) holders of real property or its part, or civil structures or their parts, owned by the State Treasury or local government units, if the possession:
   a) results from an agreement concluded with an owner, the Agricultural Property Agency of the State Treasury (now: Agricultural Property Agency), or from some other legal title, with the exception of possession by individuals of residential premises other than separate real property;
   b) is not based on a legal title, subject to Article 3 para. 2 of the Act (applicable to objects of taxation included in the Agricultural Property Stock of the State Treasury or managed by the "State Forests" National Forest Holding).

> **Note:**
>
> An owner-like possessor is a person who holds a thing as if they were its owner. So a person may be an owner-like possessor without being an owner. In some cases, independent possession can lead to the acquisition of real property by acquisitive prescription.

Very important: If the real property or civil structure is held under joint ownership or is in possession of two or more entities, then it is a separate object of taxation, and the tax obligation related to the real property or the civil structure is imposed jointly and severally on all co-owners or holders. In cases where premises are held under separate ownership, the obligation to pay real property tax on the land and that part of the building that are held under joint ownership is imposed on owners of premises **in proportion to their respective fractional holdings, i.e. the ratio of the premises' floor space to the floor space of the entire building**.

Taxable base

The taxable base is usually:

1) for land – its area;
2) for buildings or their parts – floor space;
3) for buildings **or their parts** linked to running a business activity – the value referred to in income tax regulations, established on 1 January of the tax year, which is the basis for calculating depreciation in that year, not reduced by depreciation allowances; and in the case of fully amortised structures – their value as at 1 January of the year in which the last depreciation allowance was recognised.

If the tax obligation related to real property tax on a structure arose in the middle of a tax year – the taxable base is the value that was the basis for calculation of depreciation as the date when the tax obligation arose.

Note: there are numerous specific situations where the taxable base is determined in a manner other than according to general rules specified above – they are described in the Act on Local Taxes and Charges.

Method for determining the amount of real property tax vs. the date of recognition in the tax book of revenue and expenditure

The key issue in determining when and how to recognise real property tax in the tax book of revenue and expenditure is the legal status of a taxable person obliged to pay real property tax.

For individuals obliged to pay real property tax, the tax will be determined by a decision of a tax authority competent for the location of objects of taxation. The tax is payable in instalments proportionate to the duration of the tax obligation: by 15 March, 15 May, 15 September and 15 November of the tax year.

The tax authority's decision is issued based on information that individuals must submit to the tax authority (in practice, we send such information to a relevant department in the town or gmina office). Beware: if the real property or civil structure is held under joint ownership or is in possession of **individuals and legal persons, non-corporate bodies or companies without legal personality**, with the exception of persons making up a housing community, such individuals submit a real property tax return and pay the tax **on the conditions that apply to legal persons**.

Information about real property and civil structures should be submitted on a relevant form within 14 days following the date of occurrence of circumstances justifying the origination or expiry of the tax obligation related to real property tax, or following the date of an event that has contributed to the origination of the tax obligation; and if in the middle of a tax year, the tax obligation related to real property tax expired, or an event occurred referred to in para. 3, the tax authority shall change a decision by which the tax was established.

Legal persons, non-corporate bodies and companies without legal personality, organisational units of the Agricultural Property Agency of the State Treasury (now: Agricultural Property Agency), as well as organisational units of the "State Forests" National Forest Holding are required:

1) to submit, by 31 January, to a tax authority competent for the location of objects of taxation, real property tax returns for a given tax year, on a relevant form, and if the tax obligation arose after that date, within 14 days following the date of occurrence of circumstances justifying the origination of such obligation;
2) to accordingly adjust their tax returns if an event occurs referred to in para. 3, within 14 days following the date of the event;
3) to pay real property tax in the amount calculated in the return – with no prior notice – to the bank account of a relevant gmina, in instalments proportionate to the duration of the tax obligation, by the 15th day of each month, and by 31 January for January.

Taxable persons paying real property tax on the conditions specified for legal persons

General partnerships and limited liability partnerships that pay real property tax declare the tax amount without waiting for a tax authority's decision. In this case, the tax liability arises by operation of law – on the day when an event occurs that the Act on Local Taxes and Charges associates with the origination of such liability. The Act also sets out the tax point. Usually it is the first day of the month following the month in which circumstances occurred justifying the origination of the tax obligation.

TAX ON MEANS OF TRANSPORT

Tax on means of transport is a local tax, the burden of which is born by the entrepreneurs who use the means of transport referred to in the Act on Local Taxes and Charges. Similarly to real property tax, the tax increases revenue expenditure, provided that it is appropriately documented.

What is taxable?

The tax is levied on the following means of transport:

1) lorries with a maximum permissible laden weight above 3.5 tonnes and below 12 tonnes;
2) lorries with a maximum permissible laden weight equal to or higher than 12 tonnes;
3) truck-tractors and ballast tractors adapted for the use with a semi-trailer or trailer with a maximum permissible laden weight of a vehicle combination from 3.5 tonnes to below 12 tonnes;
4) truck-tractors and ballast tractors adapted for the use with a semi-trailer or trailer with a maximum permissible laden weight of a vehicle combination equal to or higher than 12 tonnes;

5) trailers and semi-trailers which together with a motor vehicle have a maximum permissible laden weight from 7 tonnes to below 12 tonnes, excluding those that are used solely in connection with agricultural activities carried out by an agricultural tax payer;
6) trailers and semi-trailers which together with a motor vehicle have a maximum permissible laden weight equal to or higher than 12 tonnes, excluding those that are used solely in connection with agricultural activities carried out by an agricultural tax payer;
7) buses.

Determination of tax rates

Tax on means of transport is a local tax and local government authorities have broad discretion in setting its rates. However, in this respect they must consider the ceilings included in the Act on Local Taxes and Charges, and observe the minimum rates set out in the annexes to the Act. Bound rates of the tax are indexed annually. Persons responsible for keeping the books of taxable persons that pay tax on means of transport must bear in mind that the rates between individual gminas may vary considerably, and one should always properly determine the appropriate territorial competence. In matters of tax on means of transport, a competent tax authority is one whose competence covers **the taxable person's place of residence or registered office**, and in the case of a multiple-plant enterprise composed of separate organisational units – a tax authority whose competence covers a plant or organisational unit that possesses means of transport that are subject to the tax.

Important: In the case of joint ownership of a single means of transport, a competent authority is a tax authority having competence over the person or organisational unit who/that is first named in the vehicle registration card.

Taxable persons in tax on means of transport

Taxable persons are individuals and legal persons who/that own means of transport. The owner definition also includes non-corporate bodies in whose name the means of transport is registered, and holders of means of transport registered in the territory of the Republic of Poland as the means that have been entrusted by a foreign individual or legal person to a Polish entity.

Note: If a single means of transport is held under joint ownership by two or more individuals or legal persons, then the tax obligation related to tax on the means of transport is imposed jointly and severally on all co-owners.

Change of ownership

If ownership of any registered means of transport changes, the tax obligation remains imposed on the previous owner until the end of the month in which the transfer of ownership took place.

Tax point

The obligation to pay tax on means of transport arises from the first day of the month following the month in which the means of transport was registered in the territory of the Republic of Poland, and if the registered means of transport is acquired – from the first day of the month **following the month** in which the means of transport was acquired.

In the case of re-entry into service, the tax obligation arises from the first day of the month following the month in which the means of transport was re-entered into service after the period for which a decision was issued by a registration authority to temporarily withdraw the vehicle from service.

Expiry of tax obligation

The tax obligation expires at the end of the month in which the means of transport was deregistered or a decision was issued by a registration authority to temporarily withdraw the vehicle from service, or at the end of the month in which the vehicle entrustment period expired.

Obligations of taxable persons in tax on means of transport

Taxable persons are obliged:

1) to submit, **by 15 February** to a competent tax authority, the returns concerning tax on means of transport for the tax year concerned, on a relevant form, and if the tax obligation arose after that date, within 14 days following the occurrence of circumstances justifying the origination of such obligation;
2) to accordingly adjust their tax returns, if circumstances occur that contribute to the origination or expiry of the tax obligation, or if a place of residence or registered office is changed – within 14 days following the occurrence of such circumstances;
3) to pay tax on means of transport in the amount calculated in the return – with no prior notice – to the bank account of a relevant gmina.

Tax on means of transport is payable in two instalments proportionate to the duration of the tax obligation, by 15 February and by 15 September of each year.

However, if the tax obligation has arisen:

1) after 1 February but before 1 September, then the tax for the year concerned is payable in two instalments proportionate to the duration of the tax obligation:
   a) within 14 days following the day when the tax obligation arose – 1st instalment;
   b) by 15 September of that year – 2nd instalment;
2) on 1 September or later, then the tax for the year concerned is payable on a one-off basis **within 14 days following the day when the tax obligation arose**.

If the tax obligation has originated or expired during the year, the tax is determined in proportion to the number of months in which the tax obligation applied.

Exemptions

The Act exempts the following entities from tax on means of transport:

1) subject to the condition of reciprocity – means of transport held by diplomatic missions, consular offices and other foreign missions enjoying statutory privileges and immunities, or privileges and immunities under international agreements or customs, and held by members of their staff, as well as other persons equated with them, if they are not Polish citizens and do not have a permanent residence in the territory of the Republic of Poland;
2) means of transport that constitute reserves for military mobilisation purposes, special vehicles and special-purpose vehicles within the meaning of road traffic regulations;
3) vintage vehicles within the meaning of road traffic regulations.

A council of the gmina has the right to introduce other objective exemptions, subject to the conditions set out in the Act.

Note: The need to pay tax on means of transport is not dependent on the actual use of the vehicle; this obligation expires only upon deregistration of the vehicle, or when a decision is issued by a registration authority to temporarily withdraw the vehicle from service.

TAX-LIKE CHARGES

Market due

Market due is levied on individuals, legal persons and non-corporate bodies that sell in marketplaces. Market due is not applied to sales in buildings or their parts.

Marketplaces are understood as **all venues** where sales are carried out.

Exemption from market due is granted to taxable persons that pay property tax in connection with the objects of taxation situated in the marketplaces.

Visitor tax

Visitor tax is levied on individuals who stay for more than one day for tourist, leisure or training purposes:

1) in localities with favourable climatic characteristics, landscape values and specific conditions which make it possible to stay there for such purposes;
2) in localities in areas that have been granted the status of health resort protection area on the conditions laid down in the Act on Health Resort Services, Health Resorts, Health Resort Protection Areas and Health Resort Gminas.

- for each day of stay in such localities.

Visitor tax will undoubtedly be revenue expenditure if it is incurred in connection with travel for training purposes related to the business, whether the trainee is the entrepreneur or it is their employees who are trained.

Health resort tax

If it is necessary to prove that health resort tax has been debited to costs, one should follow the same procedure as is applied to visitor tax.

Health resort tax is levied on individuals who stay for more than one day for health, tourist, leisure or training purposes in localities in areas that have been granted the status of a health resort on the conditions laid down in the Act dated 28 July 2005 on Health Resort Services, Health Resorts, Health Resort Protection Areas and Health Resort Gminas. The tax is levied for each day of stay in such localities.

Note: No visitor tax is levied on persons on whom health resort tax is levied.

Stamp duty

Stamp duty applies:

1) in individual cases in the field of public administration:

   a) for performance of an official act based on an application or request;
   b) for issue of a certificate on request;
   c) for issue of authorisation (permit, licence).

2) to the submission of a document confirming power of attorney or commercial representation, or its copy extract or duplicate – in a case in the field of public administration or in judicial proceedings.

Stamp duty also applies to performance of an official act, issue of a certificate and authorisation (permit) by an entity other than a central or local government authority, in connection with public administration tasks, as well as to the submission to such entity of a document confirming power of attorney or commercial representation, or its copy, extract or duplicate.

Obligations, exemptions, and a precise determination of the stamp duty object are governed by the Act on Stamp Duty. Since the Act contains a number of subjective and objective exemptions and exclusions, I encourage you to read it.

Entrepreneurs pursuing a business activity will mostly pay stamp duty on acts related to:

a) issue of decisions and permits related to investment activities;
b) issue of decisions and permits related to environmental protection;
c) issue of decisions, permits, promises, etc. related to permits and licences to pursue a regulated and licensed business activity;
d) issue of duplicates of official documents;
e) provision of information about other business entities.

Perhaps the most frequent official act to which stamp duty applies is the issue of a tax clearance certificate or a tax arrears certificate. Then the duty is paid on each copy of the certificate.

Note: When a certificate the issue of which is not subject to stamp duty is used in a case which is subject to the duty, then the obligation to pay does arise.

The amount of stamp duty varies considerably. The assumption is that it should cover the cost of issuing the document required.

Stamp duty payers

The obligation to pay stamp duty is imposed on individuals, legal persons and non-corporate bodies, if their application or request results in an official act, or if a certificate or authorisation (permit, licence) is issued pursuant to their request; in the case of commercial representation (power of attorney, authority), the obliged payer will be a principal, an attorney, an entrepreneur or a commercial representative.

If an act that is subject to stamp duty is performed based upon a joint request (as a result of a joint application) of more than one entity, then the payment obligation is joint and several. If one party is subjectively exempt from stamp duty, then the obligation to pay rests jointly and severally with the remaining parties to the act in question.

The time at which stamp duty becomes chargeable

The obligation to pay stamp duty arises:

1) if applicable to an official act – upon making an application or submitting a request for an official act;
2) if applicable to the issue of a certificate – upon submission of a request for a certificate;
3) if applicable to the issue of an authorisation (permit, licence) – upon submission of a request for an authorisation (permit, licence);
4) if applicable to the submission of a document confirming power of attorney or commercial representation, or its copy, extract or duplicate – upon filing the document with a public administration authority, court or another entity authorised to accept the document.

If in a case that is subject to stamp duty, a certificate is used that has been issued for a case that is not subject to the duty, the obligation to pay arises when the certificate is used.

The Act provides that stamp duty is payable at the time when it becomes chargeable. In practice, entities that issue decisions, authorisations, etc. will refuse to accept documents, if no proof of stamp duty payment is provided.

Stamp duty is paid at the cashier's office of a relevant tax authority or to its bank account.

Refund of stamp duty

In some situations, stamp duty will be refunded. Refunds are always based on a taxable person's request. It is not enough for the duty to be refunded if a circumstance occurs that justifies the refund. In addition, it should be noted that the duty is not refundable after five years from the end of the year in which the payment was made.

The duty is refundable:

1) if applicable to an official act – if no official act has been performed in spite of the payment;
2) if applicable to the issue of a certificate or authorisation (permit, licence) – if no certificate or authorisation (permit, licence) has been granted in spite of the payment.

TAX OPTIMISATION

Tax optimisation vs. tax evasion: the differences

The multiplicity and complexity of taxes in Poland is very high. Of course, Poland is no exception here: tax systems in many countries are characterised by a high degree of complexity. This is because of the design of modern tax systems is meant to prevent tax evasion. However, there are at least three reasons why it will always be possible to reduce the tax burden without compromising legality.

Differences in tax systems

The first reason is that differences occur in the tax systems of various countries, such as in terms of their tax rates. The existence of so-called 'tax havens' makes it possible for a taxable person to manage their affairs in such a way that taxes are lower, despite the fact that income (or other taxable base) remains unchanged.

Such measures are most frequently referred to as optimisation measures as they are meant to avoid excessive taxation. These activities are perfectly legal, although they meet with considerable criticism. These are not cheap solutions and require the involvement of a sizeable capital. It should be mentioned that recently the euro area countries have been undertaking some intensive activities aimed at reducing, as far as possible, the opportunities to shift taxes across countries. In the near future, we should expect a legislative offensive on the part of the tax authorities. The first announcements have already been heard in Poland.

Design flaws in the tax system

If, contrary to its intention, the legislator adopts a provision allowing a reduction in tax liabilities, taxable persons may utilise such a loophole for their benefit. Some time ago we had in Poland a notorious (and gigantic) tax loophole created by a regulation on donations to individuals. The tax system is so complicated that it is difficult to avoid such errors in the legislation. However, the very fact that the provision was adopted and (as it turned out afterwards) allowed a lot of leeway in reducing the tax burden or to spread it over a long time, was excuse enough to use the opportunity while the regulation was still in effect.

Currently, there are many solutions that make it possible to minimize current tax burdens in accordance with the letter of the law. These solutions are often available for a short time only, as the legislator systematically removes all loopholes as they appear.

Intentions of the legislator

Since the function of taxes is not purely a fiscal one, but they also operate as a form of regulating measure and a stimulating factor for social and economic processes that are important for the legislator (i.e. the State). Some tax solutions are included in legal regulations that allow all taxable persons to achieve tax benefits, usually provided that they satisfy some specific conditions.

You should note that in the era when housing problems were widespread, there were also extensive tax breaks in force to stimulate the construction industry. Demographic problems in turn have contributed to the enactment of "family relief". As we now deal with a readily noticeable social security crisis, it prompts the legislator to introduce some incentives for taxable persons so that they are more willing to put aside some of their current income now to provide for the future. On the other hand, the economic slowdown prompts the legislator to introduce some pro-investment solutions or measures to increase employment.

Is tax optimisation wrong?

When we talk about avoiding the paying of taxes, we normally refer to a person who is simply a tax criminal. Meanwhile, there is a huge difference between illegal behaviours, concealment of income or income sources, etc., which all constitute **tax evasion** – an act which is a criminal or criminal fiscal offence or a petty offence and tax optimisation measures.

In contrast to tax evasion, the concept of tax avoidance should be reserved for activities aimed at a legitimate and legal reduction of the amount of taxes paid, or putting a tax payment date off to a time which is more opportune for a taxable person.

So there is a fundamental difference between tax avoidance and tax evasion: the former is about legal activities within the limits of law, often desirable by the legislator, whereas the latter is a criminal offence or petty offence, which is prosecuted and punished ex officio.

Tax optimisation areas

While discussing tax optimisation areas, we should ask ourselves a question: what do we mean by tax optimisation?

No strict definition exists. The essence of optimisation is simply the use of solutions that in a taxable person's specific circumstances will allow them to legally pay less tax, pay it at a later date, or not pay it at all.

Important: tax optimisation activities require careful planning and predicting of the consequences of tax-related decisions before they are implemented. Most frequently, when a transaction or act is already completed, optimisation becomes impossible or very difficult, and its effects tend to be less spectacular. The domain related to the analysis of future events is referred to as tax planning. By means of tax planning we prepare ourselves to optimisation our future liabilities.

Here is a simple Example:

You buy an old lamp at a flea market for 1000 PLN. It turns out, however, that it does match your interior in the way that you have expected. So you decide to put it to an online auction. Surprisingly, you obtain the price of 8000 PLN. In other words, the transaction has resulted in income being, to put it in simple terms, the difference between the purchase price and the selling price. If not more than 6 months have passed since the lamp purchase day, you will have to pay tax on that income. If you sell the lamp after 6 months, the tax will not apply.

If you are unaware of that rule before the transaction, you cannot later reverse the practical effects of your action once the transaction has been concluded. On the other hand, if you have such knowledge before, you can schedule your transaction in such a way that it takes place after the 6-month period. In this way, you will be able to legally avoid having to pay income tax on the 7000 PLN amount.

The auction example shows that the use of tax optimisation is possible for all taxable persons, regardless of income or the way it is earned. Remember, however, that effective optimisation requires knowledge, goal setting and planning. Only if you combine all these elements, will you be able to get the expected benefits within a specific time horizon.

As we have already mentioned, the legislator uses tax legislation to stimulate certain behaviours of taxable persons. The incentives can be short-term or long-term, and make it possible for taxable persons to get the benefits the value of which depends not only on the person's financial situation, but also on the use of an appropriate strategy, planning all activities in time and consistency in application of the selected measures.

Still, defining the areas of possible tax optimisation, is not only about implementing the legislator's stimulus plans. As taxable persons we are obliged to pay various types of tributes: income taxes, VAT, excise duty, local taxes, tax on civil law transactions, tax-like charges, etc. – in each of the above-mentioned tax areas, there is room for tax planning and implementation of optimisation measures with the use of the existing legal solutions.

Safety of a taxable person optimising their tax liabilities; rights of taxable persons

While talking to entrepreneurs or their accountants we often hear that they are concerned about the future impacts of their optimisation efforts. It is hardly surprising given the widely-known oppressiveness of tax authorities and publicised cases of high-profile conflicts, leading to the liquidation of successful companies that have been the subject of detailed analyses. But we should remember that one significant change has been implemented here. Now, we have an institution of individual interpretations issued for taxable persons' unique circumstances. We can obtain interpretations relating to both taxes, and other tributes, such as compulsory social security contributions. If we obtain an interpretation and adhere to it, we are on the safe side while dealing with tax authorities.

Tax optimisation solutions that we undertake are either obviously legal, and as such confirmed by numerous tax interpretations, or not – then we can apply for a case-specific interpretation, and when we do not agree with its findings, file an appeal with an administrative court. This is the last resort but sometimes it is really worth taking such action.

Administrative courts repeatedly speak on matters related to tax avoidance. Their position is that if a taxable person may choose between two legal courses of action, one of which will reduce or defer a tax liability, they have the right to do so, and tax authorities are not authorised to challenge such conduct.

But it is hard to overlook the fact that tax authorities are constantly trying to block such legal activities of taxable persons, especially when there is some kind of a mass rush leading to considerable tax savings on the taxable persons' side. However, if this is the case, the authorities' chances to win the case before court are virtually zero. This is because the correct way to impose tax burdens is to have the right wording in the laws, so legislators should shape legislation in such a way as to achieve their goals. Taxable persons are only required to comply with the applicable regulations.

Activities and measures to be avoided in order to fully and legally optimise tax liabilities

Optimisation activities are, as I have repeatedly emphasized, fully legal. However, there are many different measures that, in spite of having the same goal of reducing or deferring the obligation to pay, constitute an offence, a petty offence or at least an action that may be successfully challenged by the tax authorities. Therefore, while discussing optimisation activities that are fully compliant with law, we will also point out similar but illegal activities.

Here, it is worth quoting a quite important provision included in the Tax Code:

> **Article 199a.** § 1. While determining the content of a legal transaction, a tax authority takes into account the unanimous intention of the parties and the purpose of the transaction concerned, and not only the literal wording of declarations of intent submitted by the parties to the transaction.
>
> § 2. If, under the pretence of doing one legal transaction, another legal transaction has been completed, the tax consequences shall be derived from the concealed legal transaction.
>
> § 3 If the evidence gathered in the course of the proceedings, in particular testimony of a party, unless the party refuses to testify, raises doubts as to the existence or non-existence of a legal relationship or a right to which tax consequences are related, then the tax authority applies to a common court to establish the existence or non-existence of such legal relationship or right.

We encounter opinions that the provision quoted above gives tax authorities a lot of freedom, as they are allowed to question a number of transactions, claiming that they are fictitious.

We do not agree with this opinion. Please note that where there is no concealed legal transaction, the tax authority will not be in position to question the 'real' transaction. If it does, such a position will certainly not be defensible in a court of administration.

Still, it is us, as taxable persons, who are obliged to ensure the legality of our conduct. We cannot expect sympathy if we actually undertake transactions that are fictitious or otherwise contrary to law. Typical examples of pseudo-optimisation activities that will be instantly seized on by tax authorities include:

a) buying "shady" invoices;
b) documenting transactions that have not taken place;
c) failure to document transactions that have actually been completed;
d) understatement or overstatement of the actual value of transactions;
e) understatement of the taxable bases;
f) preparation of internal costing documents that will inflate the actual cost figures;
g) understatement of the assessment basis for social security contributions;
h) artificially inflating those salary components that are not subject to income tax and compulsory social insurance contributions;
i) underreporting tax amounts on tax returns – with the intention to correct the return at a later date and supplement the missing amount with lower interest for late payment.

This is just a handful of the numerous "solutions" employed by some entrepreneurs. They have nothing to do with tax optimisation; they are simply tax evasion measures, which, if detected and proven, can cause serious legal problems.

OBLIGATIONS OF TAXABLE PERSONS IN POLAND

Obligation to register with a tax office

Each taxable person must have their individual Tax Identification Number (NIP). A NIP is assigned by the head of a tax office and is used to register taxable persons and taxpayers. In order to have a Tax ID assigned, it is necessary to submit an identification application on a special form. Should any details of a taxable person change, such as name, residential address, places of establishment, etc., the person is obliged to notify the tax authority of such changes by submitting an update notification.

Obligation to comply with payment deadlines

A taxable person is obliged to make prompt payment of taxes. Payment deadlines depend on the way in which a tax liability arises. If it arises: by way of a decision determining the amount of tax liability – the payment deadline is 14 days from the decision service; by operation of law – the tax must be calculated and paid by a taxable person on their own – payment deadlines are specified by the provisions of individual tax statutes. The same time limits apply, if tax regulations provide so, to tax returns filings. The tax payment date is understood: in the case of cash payments – as the day when the amount of tax is paid at the cashier's office of the tax authority or to the authority's bank account: at the bank, post office or co-operative savings and credit union, or as the day when the tax is collected by the taxpayer or tax collector; in the case of non-cash payments – as the day when a taxable person's account held with a bank or a co-operative savings and credit union is debited with a relevant amount based on a transfer order.

In a situation where a taxable person fails to pay tax within the prescribed period, tax arrears arise on which interest for late payment must be calculated and paid with no prior notice. If the last day of the prescribed period is a Saturday or a public holiday, the last day of the period shall be the day following the holiday(s).

Obligation to retain records

A taxable person is obliged to retain all tax documents (bills, invoices, tax ledgers, documents related to levying or collection of taxes, etc.) until the relevant tax liabilities become time-barred. The limitation period is 5 years from the end of the calendar year in which the tax was due and payable. In certain situations, the limitation period may be suspended (such as starting from the date of a decision to spread tax payment into instalments, or the date when proceedings are instituted relating to a fiscal offence or a petty fiscal offence), or interrupted (e.g. following the application of an enforcement measure), which will also extend validity of the records retention obligation.

Obligation to notify the authority of a change of address

A party in tax proceedings or its representative is obliged to notify the tax authority before which the proceedings are pending of any change of address. If a taxable person goes abroad for at least 2 months while tax proceedings are pending, they are obliged to appoint an agent for service. If a party neglects such responsibilities, all communications shall be deemed served if served to the party's previous address.

Obligation to appear when officially summoned

A taxable person is obliged, when officially summoned by the tax authority, to provide explanations, give evidence or perform a specific act in person, through a representative, or in writing. The tax authority may accept an explanation or evidence, or perform an act at the place where a person stays, when they are unable to appear due to illness, disability or for other valid reason. The obligation to appear in person before the tax authority only applies within the limits of a voivodeship where a taxable person resides or stays, unless the nature of a case or an act requires that they appear in person before the tax authority that conducts the proceedings.

If, in spite of having been correctly summoned by the tax authority, a taxable person fails to appear in person without a legitimate reason, they may be punished with a disciplinary penalty of up to 2600 PLN.

Obligations during a tax audit

In the course of a tax audit, a taxable person is obliged within the prescribed period to give any explanations concerning the subject of the audit, provide the auditing entity with requested documents related to the subject of the audit, and make it possible for the auditing entity to perform other activities listed in the Tax Code, as well as ensure the auditing entity suitable working conditions, including, if possible, a separate room and a place to store documents. In the absence of a taxable person during the audit, they are required to appoint a person who will substitute for them.

RIGHT TO THE REFUND OF OVERPAID TAX

An overpayment arises if the undue tax was paid (i.e. payment was made in spite of the fact that there was no obligation to pay) or the payment amount was higher than required. The overpayment also occurs where a taxpayer (i.e. the employer or the pension institution) collected the undue tax, or where the collection amount was higher than the tax due.

In these situations, a taxable person has the right to ask the tax authority to confirm that there had been an overpayment of tax. The overpayment with is interest is credited ex officio towards any tax arrears, including interest for late payment, and current tax liabilities, and if no such items exist, is refunded to the taxable person ex officio. A taxable person may also request that the overpayment should be credited in whole or in part towards their future tax liabilities.

In a situation where a person is not obliged to have a bank account, the overpayment is refunded in cash. In order to obtain the refund to a bank account, a taxable person is obliged to submit to a tax office a NIP-3 (or NIP-1) form in which they indicate the bank account number. If the overpayment is refunded by postal order, any applicable postal charges are deducted from the amount.

If a tax authority defaults on the deadline for the overpayment refund, a taxable person is entitled to interest equal to the interest for late payment that is collected on tax arrears.

Right to correct a tax return

If a taxable person makes a mistake in their tax return, such as in the determination of the tax liability, overpayment or refund amount and other data in the form, they have the right to file a corrective return. The right to correct the tax return is suspended for the duration of the tax proceedings or tax audit (to the extent related to tax liabilities to which the proceedings or audit refer).

Any mistakes are corrected by submitting a corrective return along with written reasons for the correction. While submitting a corrective return, a taxable person must remember to pay any outstanding tax or return the overpayment (that was unduly recognised and the refund of which was unduly collected by the taxable person) – along with interest. If, following the document review, it turns out that a tax liability, an overpayment, a tax refund or a loss amount does not exceed 1000 PLN, and provided that the correction was necessitated by errors of calculation and obvious mistakes, the tax return will be corrected by the tax authority on its own. Then the taxable person concerned receives a certified copy of the corrective return for approval (with the right to object). If no objection is lodged, the correction made by the tax authority will bear the same legal effects as the taxable person's correction. If a corrective tax return is effectively submitted along with reasons (except for corrective returns that are submitted in connection with a tax audit or checks) and if tax arrears are paid within 7 days of filing the corrective return, a taxable person has the right to apply a reduced rate of interest for late payment (i.e. ¾ of the basic rate).

Right to request a certificate

If a specific legal provision requires an official confirmation of certain facts or legal status, or a taxable person has a legal interest in the official confirmation of certain facts or legal status, the taxable person may request a relevant certificate from the tax authority (e.g. a tax clearance certificate). The certificate should be issued not later than within 7 days. The tax authority may only issue a certificate whose content is confined to the taxable person's request.

Right to data protection

Personal details contained in tax returns and in any other documents and information submitted to a tax authority, as well as any data from files of tax cases are covered by confidentiality in tax matters. Any unauthorised disclosure of such information is subject to criminal liability.

Right to reliefs in repayment of tax liabilities

Where a taxable person settles their taxes via a taxpayer (earns income from employment, retirement pension, disability pension, etc.), they may apply to a tax authority to exempt the taxpayer (the employer, the Social Insurance Institution (ZUS)) from the obligation to collect the tax. When submitting such a request, the taxable person must demonstrate that the tax collection threatens their important interests, in particular, their existence, or provide prima facie evidence that the tax collected would be disproportionately high compared to the tax due for a tax year or another settlement period. If a taxable person pays tax advances on their own, a tax authority may also – at the request of the taxable person – limit the collection of such tax advances. The person must, however, provide prima facie evidence that the advances calculated in line with the rules specified in the tax statutes would be disproportionately high compared to the tax due on the income that the person expects to earn in a given tax year.

If some vital or public interest exists that weighs in favour of such action, a taxable person may also request the following from a tax authority: that the deadline for payment of a tax or tax arrears with interest for late payment be postponed; that payment of a tax or tax arrears with interest for late payment be spread into instalments; that tax arrears, interest for late payment or a deferral fee be remitted in whole or in part (with the deferral fee understood as the fee for benefiting from the instalment arrangement or remittance). These reliefs are granted exceptionally, only in particularly justified cases. Entrepreneurs will find a full catalogue of admissible uses of tax authorities' aid in the Tax Code.

Right to obtain a written interpretation

If a taxable person is in doubt as to how to apply tax regulations in an individual case, they may request for a written interpretation (individual interpretation). Such written interpretations are prepared by directors of tax chambers in Bydgoszcz, Katowice, Poznań and Warsaw, acting on behalf of the Minister of Finance. Before sending a request, a taxable person should check which tax chamber director is competent for the person's place of residence or registered address. The request should include a comprehensive account of the facts or a future event, and the taxable person's own position concerning the legal assessment of such facts or the future event.

A request is not allowed if: the facts of the case presented in the request are the subject of tax proceedings, tax audit or the tax inspection authority's inspection proceedings that are pending on the day when the request for interpretation is submitted, and if the essence of the case included in the request has already been resolved in a decision or a ruling of a tax or tax inspection authority.

A request for individual interpretation is subject to a fee of 40 PLN, which must be paid within 7 days of the request filing date. If a single request covers several groups of facts or several future events, then the fee is charged on each separate group of facts or each separate future event presented in the request. If the fee has been paid but was not due, then it will be refunded within not later than 7 days following the conclusion of the interpretation procedure.

Right to appoint an agent to sign a tax return

An agent may be appointed to sign a tax return. If a tax return is signed by an agent, a taxable person is relieved from the signing obligation (unless separate statutes provide otherwise).

Rights in the course of tax procedures

Right to actively participate in tax proceedings

A taxable person has the right to actively participate, in person or through an agent, at every step of the tax proceedings to which they are a party, regardless of whether they are carried out by the first or second instance body. The right survives the end of the proceedings. Consequently, a taxable person has the right to access the case files within the premises of a tax authority, in the presence of an employee of that authority, and to make notes from, or copies or duplicates of such files. In addition, they have the right to request certification of copies or duplicates of the case files, or request certified duplicates from the case files. Before a decision is made, a taxable person is also authorised to express their opinion on the evidence collected in the case within 7 days of receiving a tax authority's notice.

Right to have the case promptly processed by an authority

A taxable person has the right to expect that their case will be processed without undue delay, within the time-limit not exceeding one month, and if the case is particularly complicated – within a time-limit not exceeding 2 months following the initiation of the proceedings. A case in the appeal proceedings should be processed within a time-limit not exceeding 2 months following the receipt of an appeal by the appellate body. If a request for a hearing has been submitted or a hearing has been held ex officio, the case should be processed within the time-limit not exceeding 3 months. If a case is not processed within a specified time-limit, a tax authority is obliged to notify a taxable person to this effect, give reasons for the delay, and specify a new deadline for processing the case. Moreover, if a case is not processed within a specified time-limit or within a time-limit specified in the notice, a taxable person has the right to submit a prompt-note to a tax authority of a higher instance, or to the Minister of Finance – if it was a tax chamber that has failed to process the case on time.

Right to have the procedural time-limits restored

In a situation where a taxable person fails to meet the procedural time-limit to perform a certain act (e.g. to lodge an appeal or complaint, etc.), they have the right to request a competent tax authority to restore the relevant time-limit. The tax authority is obliged to restore the time-limit, if all of the following conditions are satisfied: prima facie evidence exists that the taxable person's failure to meet the time-limit was not by their fault; the request to restore the time-limit was submitted within 7 days following the date when a reason for failure ceased to apply; and that upon submission of the request, another act was completed for which a time-limit existed.

Right to appeal against a decision

A taxable person has the right to appeal against a tax authority's decision given in the first instance, within 14 days following the receipt of the decision, and the information on such right should be included in the decision. An appeal is lodged to a competent appellate body via the tax authority that issued the decision. The appeal should include objections to the decision, specify the essence and scope of the request that is the subject matter of the appeal, and indicate evidence to justify the request. At a reasoned request, the appellate body may hold a hearing at which the taxable person can provide explanations, submit requests, proposals and objections and present evidence in support thereof. The appeal may be withdrawn at any stage of the appeal proceedings, until the decision is made by the appellate body. The appellate body may refuse to comply with a request for withdrawal of the appeal, if it is probable that as a result of such withdrawal a decision with serious legal defects will remain in force.

A decision of the appellate body may be appealed against by the taxable person, via that body, to a voivodeship administrative court within 30 days following the receipt of the decision, and the information on such right should be included in the decision.

Enforcement of a decision

A decision that is not final and that imposes on a taxable person an obligation enforceable in accordance with the provisions of administrative enforcement proceedings will not be executed unless the decision is immediately enforceable. Immediate enforceability is imposed by way of an order about which a complaint may be made. A final decision is enforceable, unless its execution is stayed. A tax authority of the first instance stays the execution of a final decision if a complaint has been lodged to an administrative court, until the administrative court's ruling becomes final: at the request of a taxable person – following the establishment of a performance bond relative to an obligation arising from the decision, together with interest for late payment, in the form of, inter alia, a bank or insurance guarantee or a bank surety – up to the amount and for the duration of the bond; ex officio – following a valid entry of a compulsory real estate mortgage, or an entry of a tax lien, both with the priority of satisfaction, which secure performance of an obligation arising from the decision, together with interest for late payment – up to the amount corresponding to the value of the compulsory real estate mortgage or the tax lien. If the execution of a decision is stayed, it does preclude the possibility of its voluntary execution.

Right to appeal against a ruling

Similar rules apply to appeals against rulings, except that the appeal against the ruling may be lodged within 7 days following its receipt. The complaint may only be lodged if the Tax Code so provides. Information for the taxable person on the right to complain, and the time-limit and method to lodge a complaint will be included in the ruling.

Right to challenge a final decision

In a situation where a particular tax decision has become final, a taxable person has the right to request a tax authority to challenge the decision, in cases specified in the Act, and by: resumption of the proceedings, or annulment, revocation or amendment of the decision.

Specific conditions for use of each of the above-mentioned procedures are specified in legal regulations. A taxable person should select the procedure that suits the circumstances present in the case. These procedures are considered extraordinary.

Right to seek reimbursement of the proceedings costs

A tax authority is obliged, at the request of a taxable person, to reimburse the costs of the proceedings, including travel expenses related to personal appearance, if the proceedings were initiated ex officio or when a person was wrongly summoned to the tax authority. A request for reimbursement of travel expenses should be submitted to a tax authority that manages the proceedings prior to the decision in the case, under pain of losing that claim. If a tax authority has incurred the costs of the proceedings in a taxable person's interest or following their request, and such costs do not stem from the statutory obligation of the authority that manages the proceedings, then such costs may be charged to the taxable person.

Rights related to the tax audit

A taxable person should be notified of the authorities' intention to initiate a tax audit. The provisions of the Tax Code provide for exceptions, i.e. situations where a tax authority does not notify of its intention to initiate the audit. If this is the case, a taxable person is informed, once an audit is already in progress, why no audit notification has been served. The audit is initiated not earlier than after 7 days and not later than after 30 days following the service of the audit notification. Any audit before the expiry of the above-mentioned period of 7 days must be approved by the auditee. On the other hand, if the audit is not initiated within 30 days following the service of the audit notification, a re-notification is required for the audit to start. As a rule, a tax audit is initiated when the auditee receives the auditor's audit authorisation document and is shown the auditor's official ID. A tax audit authorisation document must include information on basic rights and obligations that apply during the audit. If the auditee does not agree with the audit findings, they may, within 14 days of having received the audit report, submit their reservations or explanations, while indicating appropriate motions as to evidence. The auditor is obliged to take a stance on the above.