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Recent Developments in International Taxation

Poland

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Tax landscape

In Poland, the Ministry of Finance and Parliament are continuing their vigorous efforts to prevent tax avoidance and maximise tax revenue. The collateral damage is that the Polish tax system is facing criticism within Poland and at international level. According to the 2021 International Tax Competitiveness Index prepared by the Tax Foundation, Poland was ranked 36th out of 37 countries covered by the research. The reasons for such a low assessment were that Poland suffers from continuing major tax policy changes and a distorted diversity of ideas on what and how to tax.

The year 2021 did not cause much disruption in Poland's international taxation regulations. Most importantly, a technical set of rules was introduced to govern tax collection more effectively in cases involving the indirect trading of Polish real estate.

This year did bring a large dose of tax legislation ambitiously named the Polish Deal, supposedly referring to the American reforms of the 1930s that brought the United States out of the Great Depression. It is now a common view that the 2022 tax reform failed to satisfy expectations, and many measures, tools and solutions it introduced were suspended or retracted.

From the perspective of international tax, relevant developments involve the introduction of:

- a Polish equivalent of diverted profits tax;
- a local participation exemption regulation;
- an investment agreement (special tax rulings for investors);
- a withholding tax regulation (finalised); and
- a lump sum tax for high-net-worth individuals and more.

2021

Capital gains tax on the disposition of shares in real estate companies

A new tax procedure was implemented to facilitate the collection of tax on the foreign disposition of shares in companies whose prevailing assets are directly or indirectly held real estate located in Poland with a value of at least PLN 10m.

A real estate company whose shares are disposed of must pay capital gains tax advances on behalf of its foreign tax resident shareholder whenever the sale involves shares representing at least five per cent of the target's shares, voting rights or participation.

The amount of the payable advance payment is 19 per cent of the relevant tax base. Before tax is due, the seller–taxpayer must transfer funds to the tax remitter to cover the tax advance payment and should send the package of information used to compute it. If the target does not know the value of the transaction, it must pay a tax advance payment equal to 19 per cent of the market value of the shares sold.

For tax purposes, a real estate company resident outside the European Union and European Economic Area (EEA) must appoint a tax representative to perform the duties of the tax remitter. The representative is jointly and severally liable with the real estate company for the seller's tax liability.

Hybrid mismatches

As an implementation of the EU Anti-Tax Avoidance Directive (ATAD 2), a set of new regulations addressing hybrid mismatches entered into force. The changes are intended to prevent aggressive tax optimisation taking advantage of hybrid instruments and hybrid entities. The law identifies potentially abusive arrangements and prevents tax savings related in particular to the recognition of tax-deductible expenses within double deduction arrangements, recognition of tax-deductible expenses in the case of deduction without taxation, non-recognition of revenue in the case of deduction without taxation and advantage taken of an abusive hybrid structure mismatch, as well as double recognition of withholding tax relief.

2022

Diverted profits tax

A new diverted profits tax is imposed on Polish taxpayers and foreign taxpayers with a permanent establishment in Poland who incur expenses directly or indirectly towards their related parties when such expenses are considered an abusive shifting of profits to low-tax jurisdictions.

A 19 per cent tax applies to expenses for intangible services (consulting, market research, advertising, management and control, data processing, insurance, guarantees and warranties, and similar), as well as fees and charges for the use or right to use copyrights, licenses, industrial property rights and know-how.

The tax is also charged on expenses for the transfer of the risk of insolvency of the debtor under loans other than those granted by banks and cooperative savings and loan associations, costs of debt financing, and fees and remuneration for the transfer of functions, assets or risks.

Diverted profits tax applies if:

- the expenses listed above (including expenses incurred towards unrelated parties) in total exceed three per cent of total taxpayer tax-deductible expenses in a given tax year;
- the related party paid an effective income tax of less than 14.25 per cent in a given tax year; and
- the payments constituted mostly of the related party's revenue, whereas such revenue reduced the taxable basis of that related party or was redistributed in the same year.

The tax does not apply to transactions with EU and EEA tax residents who engage in real substantial economic activities in their countries of tax residency.

The regulation provides for limited deductions to mitigate double taxation.

Diverted profits tax together with minimum income tax and the hidden dividend regulation constitute an anti-tax abuse package that is a substitute for the historical limitation of tax expense deductibility. Due to concerns related to the application of the new law, the hidden dividend has been immediately suspended and is likely to be abolished, while two remaining regulations will be amended by the end of the year.

Local participation exemption regulation

A new tax regime for holding companies with participation of at least ten per cent in Polish or foreign subsidiaries allows:

- the exemption of 95 per cent of dividends they distribute from tax; and
- the exemption of the disposition of the subsidiaries' shares to an unrelated party from capital gains tax.

An exemption from capital gains tax is the core benefit of the new rules, but comes at the price of giving up the full dividend tax exemption available under the EU-law driven participation exemption.

The benefit from the regime is subject to a number of restrictions:

- the parent must engage in participation in the subsidiary for at least one year;
- neither the parent nor subsidiary can belong to a tax capital group or benefit from a corporate income tax exemption in the form of public aid;
- the parent must run a genuine business;
- the holding company cannot be owned directly or indirectly by an entity from a tax haven or country with which Poland cannot exchange tax information under treaties, while the subsidiary cannot be located in any such country;
- the subsidiary is subject to tax on its global income and does not take advantage of an exemption from tax; and
- the subsidiary cannot hold more than five per cent of shares in another company and does not engage in participation in investment funds and the like or partnerships, and is not entitled to benefits as a founder or beneficiary of any fiduciary institution.

Finally, the capital gains tax exemption does not apply to dispositions of shares in a real estate company, that is, whose assets directly or indirectly mainly consist of real estate located in Poland.

In turn, the close-to-exemption from the taxation of dividends does not apply if a significant portion of a foreign subsidiary's earnings consist of selected types of active and passive low-taxed income (unless it is a tax resident in the EU or EEA running a genuine business there), otherwise the dividend exemption would result in a hybrid mismatch. Following the expected amendments, this regulation is likely to allow the full exemption of dividends from tax.

Investment agreement (special tax rulings for investors)

Wary of the instability of Polish tax law and its interpretations, and the need to increase the share of foreign investment in the production of gross domestic product, legislators introduced a new tool for investors to manage their tax risk.

An investment agreement between an investor and the Ministry of Finance is meant to provide complete official guidance in terms of any tax consequences of a planned investment. It is binding for the investor, Minister of Finance and tax authorities.

An investment agreement may secure the taxpayer's position in various fields:

- transfer pricing (an advance pricing agreement);
- confirming the absence of tax avoidance (a general anti-tax avoidance regulation clearance opinion);
- excise (an individual excise ruling); and
- VAT (an individual VAT rate ruling);

and other tax consequences related to an endeavour (an individual tax ruling).

An application can be submitted by an investor or group of investors, in particular a consortium, company, branch or representative office formed in connection with an investment. To be eligible for a ruling, an investor must spend approximately €10m (€20m until 31 December 2024) to acquire tangible or intangible assets in connection with a new or existing establishment.

The application fee for a ruling is approximately €10,000 per investor. The main fee of between approximately €20,000 and €100,000 payable upon completion of a ruling depends on the complexity of a case and may be subject to negotiation.

An investment agreement is meant to ensure long-term guidance and may therefore be valid for up to five years.

Withholding tax regulation (finalised)

A new regulation governing obligations related to withholding tax by Polish tax remitters was introduced at the start of 2019. The reform modified the definition of 'beneficial owner' by adding a condition to the effect that, to be considered a beneficial owner, an entity must actually be conducting business in the country of its registered address if it receives payments related to such business.

Apart from that, the mechanism for applying a withholding tax exemption or reduced tax treaty rates has been changed from relief at source to pay and refund. This new mechanism was controversial even before it entered into force. Hence, its application was suspended (with some exceptions) until 2022.

Currently, if payments (eg, dividends, interest and royalties) to a single related-party taxpayer are subject to withholding tax and exceed PLN 2m (approximately €400,000) in a single year, the tax remitter should withhold tax on the excess over this amount at the statutory rate. The refund is processed in a dedicated procedure.

Alternatively, a tax remitter may apply an exemption or reduced tax rate according to a double taxation prevention treaty if the tax remitter conducted a survey and is able to state that it 'does not possess any information justifying a suspicion that there are circumstances excluding the possibility of applying a [reduced] tax rate or not charging withholding tax'. An individual who makes a false statement may be held liable for a criminal offence, while an additional penalty tax obligation may apply to the tax remitter.

An alternative is to apply to tax authorities for an official opinion confirming the correctness of the application of a withholding tax exemption or reduced tax treaty rate.

Lump sum tax for high-net-worth individuals

Poland joined a group of countries offering special tax treatment to high-net-worth individuals. Foreign taxpayers who change their tax residency to Poland can opt for an annual lump sum tax of PLN 200,000 (approximately €40,000) on their entire foreign income, except for controlled foreign entity income, while income earned from Polish sources is taxed on a regular basis.

The taxpayer is blessed with a low degree of disclosure obligations without having to report the source and amount of foreign income. However, the taxpayer must be able to provide such information at the request of the tax authorities.

Lump sum taxation is available to those who:

- have not been a Polish tax resident for five years during the last six years; and

- invest PLN 100,000 per year (approximately €20,000) in Polish economic growth, development of science and education, protection of cultural heritage or promotion of physical culture.

A taxpayer can benefit from lump sum taxation for ten years. Close relatives of taxpayers may opt in to lump sum taxation at the price of PLN 100,000 annually (approximately €20,000).

Tax benefit for taxpayers returning to Poland

A tax benefit has been introduced to encourage private individuals to move their tax residency to Poland. New taxpayers will be entitled to take advantage of a personal income tax-free amount of PLN 85,528 on their employment (and similar) and private business income. The benefit will be available for four consecutive years.

The benefit is available to persons who have not been Polish residents for at least three preceding years and:

- have Polish citizenship, hold a Polish Card (confirming Polish nationality), or have citizenship of another EU/EEA Member State or Switzerland;
- lived for at least three preceding years in an EU/EEA Member State, Switzerland, Australia, Chile, Israel, Japan, Canada, Mexico, New Zealand, South Korea, the United Kingdom of Great Britain and Northern Ireland or the US; or
- had previously lived for at least five consecutive years in Poland.

The benefit applies to taxpayers who moved to Poland starting from 2022.

Controlled foreign entity/controlled foreign corporation (CFC) rules (amended)

The controlled foreign entities regulation that was last significantly amended in 2019 has yet again undergone changes in 2022. The law that obliges Polish resident taxpayers, both corporate and personal, to include income in their tax base that was earned by a controlled entity with a seat or management in a jurisdiction with a lower level of taxation has now been extended. More entities will now fall under it and more types of transactions will trigger the application of CFC rules.

Unchanged in the regulation is that the existence of a foreign controlled entity is recognised when such an entity is located in a tax haven or jurisdiction that does not have a treaty with either Poland or the EU that allows an exchange of tax information.

The third type of controlled foreign entity now more easily attracts Polish control, and revenue collection from intangible services, leasing and conduit intercompany transactions as well as passive income in an appropriate proportion to total income can now trigger the application of CFC taxation.

The existence of the fourth type of controlled foreign entity largely depends on a disproportionate relation between significant assets that produce passive income held by such an entity and moderate revenue qualified as passive income and remuneration for intangible services.

The fifth and final type of foreign entity is recognised when the income of a controlled foreign entity is disproportionately high compared with its assets and payroll, and such excessive profit can be attributable to the significant value of transactions with related parties.

Tax treaties

Tax treaties with Malta and the Netherlands were amended and their amended shape will fully enter into force at the start of 2023.

For both tax treaties, the most relevant change is the introduction of a clause governing the recognition of gain on the disposal of shares of a company or other entity whose assets directly or indirectly primarily consist of real estate. In principle, the right to recognise gain will now lie with the country where the real estate is located and not exclusively with the country of the party disposing assets.

A protocol to the tax treaty with the Netherlands additionally changes provisions on the recognition of a permanent establishment, introduces a principal purpose test clause and a transparent entity clause, and changes the withholding taxation rules. A protocol to the tax treaty with Malta introduces changes, among others, to the taxation of royalties and director fees, and introduces a principal purpose test clause.

A tax treaty protocol was also signed with Guernsey with the intended effect of adjusting the existing tax treaty to the multilateral instrument and Polish tax policy.

According to information provided by the Ministry of Finance, in 2021 and 2022, the multilateral instrument began to fully apply in relations with Latvia, Qatar, Saudi Arabia, Russia, Cyprus, Portugal, Indonesia, Czechia, South Korea, Kazakhstan, Bosnia and Herzegovina, Albania, Jordan, Egypt, Chile, Pakistan, Estonia, Croatia, Hungary and Greece, and is expected to soon apply to Spain.

The position of the Polish Government on Organisation for Economic Co-operation and Development (OECD) Pillar 1 and Pillar 2

As a member of the OECD/Group of Twenty (G20) Inclusive Framework for base erosion and profit shifting (BEPS), Poland supports the introduction of Pillar 1 and Pillar 2. Poland would like the introduction of the two Pillars to be linked. The Polish authorities fear that processing them separately may result in the introduction of Pillar 2, with Pillar 1 being dropped due to the conflicting interests of selected international partners. This could have a detrimental effect on Polish investment incentives and deprive Poland of the benefits of Pillar 1. On 17 June 2022, the Council of the EU held a meeting of the Economic and Financial Affairs Council (ECOFIN), where the representative for Poland stated that relevant assurances for a link between the introduction of the two pillars had been given, and that Poland was ready to put aside its objections and support the directive.