

Tax Newsletter



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Dear Sir or Madam,

In this issue of the Tax Newsletter we present our commentary on VAT taxation on account of imported services. This matter is a subject of frequent enquiries, so in order to systematize and sum up tax implications in this regard we have prepared for you a practical commentary. We would also like to inform you about an important decision of the Supreme Court of Administration pertaining to the taxation of income on account of employee share schemes. We hope that this favourable decision will help tax authorities to develop a uniform approach as regards establishing sources of income and the tax point in the case of a gratuitous acquisition of employee shares.

We would also like to point enterprises acquiring intangible performances from related entities to the ongoing works of the OECD aimed at regulating these issues in a more comprehensive manner.

We encourage you to familiarise yourself with the topics discussed in this issue.

Krystyna Szydłowska

EDITORIAL

IN THIS ISSUE

- ➔ VAT: Tax Obligation on Account of Imported Services p. 2
- ➔ CIT/PIT: Opportunity to Recover Overpaid Income Tax p. 4
- ➔ CIT/Transfer Prices: OECD – After Restructuring Know-How Is on the Carpet p. 5
- ➔ PIT: Planned Changes Concerning Business Trips p. 7

VAT: Tax Obligation on Account of Imported Services

Due to a growing share of services rendered by foreign contracting parties, taxpayers have frequently doubts as to the correct establishment of the tax point for imported services. Trying to meet your expectations, we have prepared a brief study on tax implications in the case of this kind of services.

Taxpayers acquiring services from persons or entities which do not have their seat, permanent place of residence or permanent place of business within Republic of Poland are obliged to settle VAT on account of these services. In this case activities performed are classified as import of services, i.e. as a specific type of transactions, because it is the customer that settles output VAT on this account. The situation is identical when a foreign contracting party has a permanent place of business in Poland, provided that this place of business does not participate in the service provision.

In accordance with the disposition of Article 19 sec. 19 of the Tax on Goods and Services Act, provisions of Article 19 sec. 1, 4, 5, 11, 13 item 1b and 1c, item 2, 4 and 7-9 and sec. 14-16, which regulate tax point for services provided, are applied as appropriate to import of services.

The general rule as to the establishment of the tax point pertains to customers which have their seat or permanent place of residence in Poland and which are taxpayers. **In the case of imported services the tax point arises in general upon their provision.**

The general rule encompasses also situations in which a taxpayer settles a part of the payment due for the services rendered prior to their provision. This applies in particular to prepayments, advances, earnest money and instalments. In this case the tax point arises upon settlement of a part of the payment.

In situations where:

1. in connection with provision of services there are established consecutive payment or settlement deadlines, services as considered provided upon the lapse of each period to which such settlements or payments pertain until completion of service provision;
2. services are provided in a continuous manner for a period exceeding one year and thus in the given year there expire no settlement or payment deadlines in connection with their provision, services are considered provided upon the lapse of each tax year until completion of their provision;

In order to establish the tax point in a correct manner, it is very important to determine the service provision date, which may arise from the relevant agreement entered into by the parties. In the case of imported services for which the place of performance is established in accordance with the general rule (i.e. it is assumed that the service is rendered at the seat or in the place of residence of the customer being a taxpayer), the tax point does not depend on when the foreign service

provider issues the relevant invoice, but exclusively on the service provision date, lapse of the settlement period or the payment date, whichever is earlier.

Services whose place of performance is not established according to the seat, permanent place of residence or permanent place of business of the purchaser being a taxpayer are governed by other principles with regard to the establishment of the tax point.

In this case the tax point arises upon service provision. If service provision is to be confirmed by an invoice, the tax point arises upon its issuance, however not later than on the 7th day as from service provision. This applies as appropriate to invoices for a partial provision of services.

If a taxpayer settled a part of the payment due prior to the service provision, in particular in the form of a prepayment, advance, earnest money or instalment, the tax point for imported services arises upon settlement of that part.

Among services for which the aforementioned solutions with regard to establishment of the tax point apply there are: lease of real estate, transport of passengers, admission to cultural, sports and scientific events, admission to fairs and exhibitions, restaurant services and services related to catering as well as short-term car lease services.

Please note that as regards transport of passengers there is also another solution, under which the tax point arises upon settlement of the payment due in whole or in part, however not later than until the 30th day as from the service provision (regulations stipulating the tax point for domestic services of this kind apply as appropriate).

CIT/PIT: Opportunity to Recover Overpaid Income Tax on Account of Employee Share Schemes

Expanding on the subject of employee share schemes discussed in the December issue of the Newsletter, we would like to draw your attention to a recent decision of the Supreme Court of Administration¹ pertaining to this issue.

In the said decision the court ruled that gratuitous acquisition of employee shares does not result in income on account of employment relationship already upon receipt of the shares. In the opinion of the court, income may arise only upon disposal of such shares.

It is worth noting that in the practice of tax authorities there have occurred interpretations which ordained to treat the value of shares allotted to employees on a gratuitous basis (or at a discount price) as income on account of employment relationship². If an employer followed these interpretations, the value of the shares acquired/taken over by employees was added to their income on account of employment relationships, and the employer acting as a tax withholding agent was obliged to withhold advances towards PIT on this account.

The Supreme Court of Administration questioned this stance of the tax authorities. In the opinion of the court only income whose source is the employment relationship between an employee and an employer may be treated as income on account of employment relationship. If shares are granted only incidentally to the employment relationship (i.e. when they are allotted not directly by the employer, but by another entity from the capital group), then the value of the shares may not be treated as income on account of employment relationship.

The discussed decision of the Supreme Court of Administration gives an opportunity to apply for reimbursement of personal income tax overpayment in cases in which the value of shares allotted to employees within the framework of incentive schemes was treated as income on account of employment relationship and taxed upon their allotment. At your request we would be willing to verify and discuss with you practical possibilities to recover the tax paid in your specific case.

¹ Decision of the Supreme Court of Administration of 27 April 2011, II FSK 1410/10

² Cf. Individual Interpretation of the Head of the Tax Chamber in Warsaw of 27 April 2010, IPPB2/415-37/10-4/AS, Individual Interpretation of the Head of the Tax Chamber in Katowice of 8 June 2010, IBPBII/415-694/10/MM

Transfer prices/CIT: OECD – After Restructuring Know-How Is on the Carpet

In July of the previous year, after years of intensive work and multilateral consultations, in particular with business milieus, the OECD published an update of the OECD Transfer Pricing Guidelines for Multinational Enterprises and Tax Administrations.

Major changes were introduced in the first three chapters of the OECD Guidelines pertaining to the market price principle, transaction comparability analysis and application of the transaction profit method. Additionally, a new Chapter IX was introduced, which regulates some aspects of enterprise restructuring from the point of view of transfer pricing and contains among others recommendations as to transfer of functions, risks, assets and profit potential within a group of related entities.

Now works of the OECD concentrate on regulating issues concerning intangibles, which due to insufficient guidelines as to their definition and measurement for the purposes of transfer pricing constitute in practice a problematic area.

Problems with Measurement

As regards measurement, the general principle arising from agreements on avoidance of double taxation and national tax regulations is of course the market price principle. When it is know-how that is made available, the price subject to the market price analysis has the form of licence fees. Therefore, some generally used methods, which are also recommended in the OECD Guidelines, are applicable only to a limited extent. This pertains in particular to the comparable uncontrolled market price method, the resale price method and the reasonable margin method. As regards the first method listed above, limitations result first of all from the uniqueness of the know-how that is made available, which consequently makes it difficult to find a comparable equivalent. Moreover, access to data on the amount of licence fees that could be used for this purpose is restricted as well.

For this reason, the two most frequently applied licence fee valuation methods selected upon a functional analysis are the profit split method and the transactional net margin method. In practice also methods not named in the OECD Guidelines are used (e.g. income method).

Know-How or Services

In the case of transactions concluded between related entities consisting in support in the operating activity by way of provision of specialist knowledge and developed tools, it may be problematic to distinguish whether we deal only with provision of services or rather provision of know-how in the field of the pursued industrial, commercial or scientific activity, licence fees on account of which are subject to withholding tax.

Identification of the actual nature of a given transaction is the key from the point of view of the proper application of the relevant tax regulations. What decides here is the contents of the agreement, which should clearly specify the detailed scope and type of works constituting the

object of the transaction. If the performance of the analysed agreement consists predominantly in engaging appropriately qualified persons who share their knowledge and experience within the framework of on-going cooperation, than the transaction consists in provision of consultancy services. On the other hand, transactions involving provision of know-how are characterised among others by the fact that the agreement contains confidentiality clauses with regard to the disclosed information and premises implying that the provided knowledge has a specific form, e.g. is selected and documented with the use of appropriate carriers. These elements are crucial, which finds its confirmation in the definition of know-how applied in the legislation of the European Commission: it refers to „*a set of technical information that is secret, substantial and identified in an appropriate form*”. The Supreme Court of Administration cites this definition in its decisions (cf. file no. III SA 1661/02). Its explication finds its reflection also in interpretations of tax authorities (cf. interpretation of the Tax Chamber in Warsaw of 23 April 2009, file no. IPP-B5/423-47/09-2/PS).

Therefore, we would like to draw your attention to the fact that it is necessary to analyse agreements with related entities which you conclude or perform from the point of view of identification of components specific for know-how and provision of services, which allows their proper taxation. We will inform you on the progress of the OECD works as regards provision of services and intangible performances within related entities.

PIT: Planned Changes Concerning Business Trips

The Ministry of Labour is working on replacing the current ordinances regulating the principles of settling business trips with a single common act covering domestic as well as foreign business trips.

The suggested amendments provide among others for an increase in the daily allowance rates for business trips and accommodation limits. In the case of domestic trips it is assumed that the daily allowance rate will be increased from PLN 23 to PLN 30. Daily allowance rates for foreign trips will be specified in an appendix to the ordinance. The planned change in the rates varies depending on the country of an employee's stay.

The ordinance contains also regulations providing for reimbursement of business trip costs incurred by an employee in situations in which due to a fortuitous event an employee is unable to present tickets or bills confirming the expenses incurred during a business trip (e.g. when they have been lost or destroyed).

Another novelty is that the ordinance will provide for the possibility of making a foreign business on a motorcycle.

For the time being the draft is at the stage of interministerial consultations and awaits opinions of the business milieu. If the ordinance is adopted as planned, the new business trip settlement principles will come into effect on 1 January 2012.

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