

Tax Newsletter

Issue # 23 – February 2012



Dear Sirs,

We are pleased to present our February issue of Tax Newsletter. We recommend reading the article concerning an important judgment delivered by CJEU on the obligation of possession of acknowledgement of receipt of a correction invoice and its practical implications.

Moreover, we give an outline of new transfer pricing regulations introduced in Russia this year.

In this issue you will also find information regarding the regulation on business travels planned for the second half of 2012 and discussion of the Supreme Administrative Court judgement on tax treatment of interest on credit contracted for dividend payment.

We also invite you to participate in the 2012 Taxes Conference organized by Tax Advisory Department which will be held on 23 February 2012. For detailed programme of this event, please visit Mazars website at www.mazars.pl (News/Events).

Yours sincerely,
Krystyna Szydłowska

SUMMARY

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1 VAT: Judgment of the CJEU regarding the confirmation of receipt of correction invoices

On 26 January 2012 the Court of Justice of the European Union passed a judgment concerning the Polish regulations by which it ruled that the requirement of the possession of confirmation of receipt of a correction invoice in order to reduce the VAT due if the price of goods or services is changed, is, in principle, consistent with the EU legislation.

In accordance with article 29 section 4a of the Act on VAT, the taxpayer is entitled to reduce the taxable base if, before the expiry of the deadline for submission of tax return for a given settlement period in which the taxpayer received the correction invoice, he is in possession of acknowledgement of receipt of the correction invoice by the purchaser of goods or services for which the invoice had been issued. Obtaining the acknowledgement of receipt of correction invoice by the purchaser of goods or services after the deadline for submission of tax return for a given settlement period entitles the taxpayer to take into account the correction invoice for the period in which such acknowledgement was obtained.

In practice, the obligation of possession of acknowledgement of receipt of the correction invoice by the purchaser is very inconvenient for taxpayers because establishing on what date the acknowledgement of receipt was received involves extra workload and administrative costs.

Therefore, in practice it was often argued that article 29 section 4a of the VAT Act is too rigorous and is against the essential construction principles of VAT. A similar approach was presented in several judgments of administrative courts (judgment of Voivodship Administrative Court in Warsaw of 31 March 2010, ref. no. III SA/Wa 2100/09; judgment of Voivodship Administrative Court in Białystok of 22 December 2010, ref. no. I SA/Bk 483/10). With regard to divergences arising from interpretation of article 29 section 4a of the VAT Act, the Supreme Administrative Court referred a question for a preliminary ruling to

CJEU concerning the conformity of the aforementioned regulation with EU VAT Directive.

In its judgment of 26 January 2012 (C-588/10) the Court ruled that the requirement imposing on the taxpayer the possession of confirmation of receipt of a correction invoice by the purchaser of goods or services constitutes a condition in the meaning of article 90 section 1 of the Council Directive 2006/112/EC of 28 November 2006 on the common system of value added tax. However, the Court also stated that **if it is impossible or excessively difficult for the taxpayer who is a supplier of goods or services to obtain such acknowledgement of receipt within a reasonable period of time, the taxpayer cannot be denied the opportunity of establishing by other means that he has taken all the steps necessary in the circumstances of the case to make sure that the purchaser of goods or services is in possession of the correction invoice and is aware of it and also that the transaction was in fact carried out in accordance with the conditions set out in the correction invoice.**

This means that a taxpayer – despite not having the acknowledgment of receipt of the correction invoice – is entitled to reduce the turnover, if he proves that despite the efforts taken he did not manage to obtain the acknowledgment of correction invoice.

However, a question arises how to interpret the general clauses used by the Court “reasonable period of time” and “all the steps necessary in the circumstances of the case”, and consequently what circumstances can be considered to be justifying the impossibility or excessive difficulty in obtaining the acknowledgment of receipt of a correction invoice by the taxpayer. Another issue that raises serious doubts is the deadline for reducing the VAT due – the Court did not state clearly whether a taxpayer not having the acknowledgment of receipt but having proved the impossibility to obtain it within a reasonable period of time is entitled to reduce the tax due in the period in which he effected the sale or whether adjusting turnover on a current basis is acceptable.



2 Transfer pricing: New transfer pricing regulations in Russia

On 1 January 2012 regulations adopted in 2011 increasing significantly the scope of controlled transactions and disclosure and documentation requirements related mainly to transactions concluded by Russian companies with local and foreign related entities entered into force in Russia.

New regulations define **types of transactions which will be subject to control with regard to transfer pricing**, focusing, to a greater extent than ever before, on transactions between related parties.

With regard to international transactions, the following are subject to control in the area of transfer pricing:

- Transactions between related entities (regardless of the transaction value);
- Transactions with foreign entities with their seats in countries listed as countries applying harmful tax competition, if the annual revenue from transactions with such entities exceeds RUB 60 million;
- Transactions concerning trade of goods such as oil, oil derivatives, metals, manure salt, precious stones and metals, if the total annual revenue from transactions concluded with same contractor exceeds RUB 60 million.

As for local transactions they will be subject to control in the following cases:

- If the total revenue from transactions concluded with the related local entity exceeds RUB 3 billion in 2012 (RUB 2 billion in 2013; RUB 1 billion from 2014);
- If the subject matter of a transaction is subject to mineral tax (calculated according to the value of mineral resources);
- If one party to the transaction benefits from tax exemptions and tax credits (e.g. as an entity operating within the special economic zone (from 2014) or a participant of the projects of "Skolkovo" innovation centre) and the value of transactions in a given year exceeds RUB 60 million;

- If one party to the transaction applies special taxation rules as a taxpayer of single farm tax or single tax on imputed income, and the value of transaction exceeds RUB 100 million (transactions will be treated as controlled starting from 2014).

Under new regulations related entities are defined as entities which hold (directly or indirectly) more than 25% (formerly 20%) of shares in the equity of another entity or are empowered to decide on the appointment of 50% of management board or supervisory board of another entity or have an impact on the conditions of transactions concluded between these entities.

Methods of determining transfer pricing

The amendments to the regulations make the Russian legislation close to the ones applicable in OECD countries, among others within the scope of transaction valuation methods. They provide for the following 5 methods:

1. Comparable Uncontrolled Price method;
2. Resale Price method;
3. Cost Plus method;
4. Comparable Profits method;
5. Profit Split method.

In the case of one-off transactions it will be possible to determine the price based on the independent expert's valuation.

Documentation and disclosure requirements

New Russian regulations introduce statutory thresholds for the value of controlled transactions, the excess of which in a given year gives rise to an obligation of preparing tax documentation to be presented on tax office's request. These thresholds equal respectively in 2012 – RUB 100 million, in 2013 – RUB 80 million. Starting from 2014 all transactions considered to be controlled will be subject to documentation obligation.

This documentation should be presented within 30 days after receiving a relevant request which can be made at the earliest on 1 June of the following fiscal year (hence, new regulations provide for a 5-month period for its preparation). These regulations do not specify however the scope of information that should be included in the documentation.



Apart from demonstrating arm's length nature of concluded transactions in the documentary evidence, Russian entities will be obliged to provide offices with information about transactions subject to control, the value of which exceeds RUB 100 million. The information specifying in particular the subject matter, parties and value of transactions carried out in a given year should be filed with the office by 20 May of the following year.

Penalties

If the tax authorities consider that the prices applied by taxpayer are not consistent with arm's length principles and he does not provide relevant documentary evidence, Russian authorities will be entitled to apply penal tax rate on underestimated or non-disclosed income. However, taxpayers have time to adapt to new regulations because the 40% rate (not less than RUB 30 thousand) will only be applicable from 2017. Until that time normal tax rates will be applied and in the years 2014-2016 a reduced penalty rate of 20% will be used.

Failure to fulfil reporting requirements, i.e. failure to meet the deadline or submission of non reliable information on controlled transactions to tax authorities can be punished with a fine of RUB 5 thousand.

Moreover, new regulations specify rules regarding:

- An institution of advance pricing agreements (APA) available only to "large" local companies;
- the possibility to make a mutual correction with another party to the transaction, if the price is adjusted following a control (only with regard to local entities and transactions);
- carrying out of analyses of market conditions of a transaction (including source of data and conditions of transaction comparability);
- control in the area of transfer pricing (for instance, a period of 3 years for performing a control starting from 2014 with maximum standard duration of 6 months).

The aforementioned changes in the applicable regulations are undoubtedly crucial for Russian taxpayers but Polish entrepreneurs concluding transactions with Russian contractors (in particular related entities) should also verify transaction valuation methods etc. from this angle.

3 PIT: New draft regulation on business travels

A draft regulation on the value and conditions of determining compensation of employees working for the central government or self-government budgetary units for business travels in Poland or abroad has been published recently on the website of the Ministry of Labour and Social Policy. Its entry into force is planned in September this year.

At present two separate regulations governing the rules of determining business travel allowance in Poland and abroad are in force.

The obligation of applying the above regulations is imposed on employers from government budgetary units and those who had not regulated the issue of business travels by internal provisions (i.e. internal rules and regulations or a collective labour agreement) or under an employment agreement – if an employee is not subject to collective agreement and the employer is not under obligation to establish remuneration rules and regulations. However, the amounts of allowances defined in internal regulations or employment agreements cannot be lower than the amounts determined for budgetary unit employees. Please bear in mind that if internal regulations or employment agreement provide for more advantageous conditions of determining business travel allowance for employees the amount of benefits actually granted to employees will be tax free and will not constitute basis for social security contributions only up to the amount of allowance defined in line with the above-mentioned regulations.

The draft regulation regarding business travels will not cause a significant rise of allowances – daily allowance is to be increased by PLN 7, from PLN 23 to PLN 30 per day of travel. As a result, lump sums calculated on the basis of daily allowance will slightly increase, i.e. fixed sum for public transport (from PLN 4.60 to PLN 6) and fixed sum for accommodation (from PLN 34.50 to PLN 45).

This draft regulation introduces a possibility of paying a partial allowance to employees travelling on business in Poland if the employer provides some meals (the amount of daily allowance is



reduced by the cost of meal received free of charge respectively by 25% - for breakfast, 50% - for dinner, 25% - for supper) – before such option was available only for business travels abroad.

As far as international travels are concerned, the draft provides for the increase of daily allowances and accommodation limits for most countries as well as change of currency (from USD to EUR). The change of allowance amounts will have a positive impact not only on compensation due to international business travels but also on the amount of PIT exemption to which Polish tax residents staying temporarily abroad and earning income from work are entitled, this exemption being calculated according to 30% of daily allowance per each day of stay in a foreign country.

Another change relating to international travels consists in the possibility of determining more than one target country. This change would allow eliminating doubts surrounding the method of determining daily allowance when an employee executes official orders in two or more countries (meant as target not transit countries).

Pursuant to the draft the regulation should enter into force on 1 September 2012.

4 CIT: Expenses for interest on credit contracted by a limited liability company for dividend payment cannot be treated as tax deductible costs

Pursuant to the resolution of the Supreme Administrative Court of 12 December 2011 (II FPS 2/11) expenses related to interest on credit contracted for payment of dividend to company's shareholders cannot be treated as tax deductible costs in accordance with article 15 section 1 of the Act on Personal Income Tax of 15 February 1992 (hereinafter "PIT Act").

In the factual situation giving rise to delivering the above judgement shareholders planned to adopt a resolution on profit allocation. Despite generating positive financial result the company did not have enough own funds to pay out dividends without running the risk of upsetting financial liquidity of the company, so the only solution was to contract a credit for this purpose.

The application for individual interpretation was lodged by the company with the aim of confirming that expenses incurred for contracting and service of credit intended for dividend payment are strictly related to the company's operation and business activity. Moreover, pursuant to the Act of 15 September 2000 – Commercial Companies' Code (hereinafter: "KSH"), the shareholder has the right to decide on dividend payment if conditions set out in articles 191-193 KSH are met, whereas the company has the obligation to pay out dividend to the shareholder.

The Applicant argued that the failure to pay out dividend on time would be the source of shareholder's claims for payment of dividend, default interest and damages for improper performance of the obligation to pay out dividend.

Consequently, according to the company the dividend payment obligation did not differ from other company's commitments, e.g. commitments to suppliers, so its proper performance was necessary from the point of view of its business activity.

In the individual interpretation, the Minister of Finance considered the company's position to be incorrect. According to the tax authority the payment of dividend could not be classified as an expense providing a source of income and was not related to maintaining or securing a source of income. Consequently, the tax authority stated that expenses related to credit for dividend payment cannot be classified as tax deductible costs.

According to the Minister of Finance, obtaining of funds for dividend payment is directly related to distributable profit, i.e. concerns the part of earned income which after CIT taxation is to be distributed among company's shareholders.

Therefore, **expenses relating to credit contracted for dividend payment (commissions, interest, etc.) being related to the category of non deductible costs cannot be treated as tax costs** in accordance with art. 15 section 1 of the CIT Act. An analogous approach was adopted by the Supreme Administrative Court.



Events Upcoming

We are pleased to invite you to business breakfasts and seminars conducted by tax experts of Mazars:

23 February 2012, 9.30 a.m.- 1:30 p.m., Mazars office in Warsaw, ul. Piękna 18

“Taxes 2012” Conference VAT/CIT/PIT changes in legislation, case law, practice

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