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# Tax Review

Dentons Poland

OCTOBER 2015

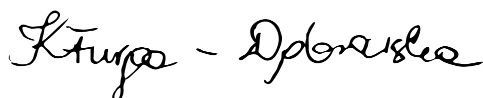
# Note from the editor

Dear Sirs,

We are proud to present the next edition of our "Tax Review" which contains a selection of rulings and interpretations that had been issued or published in September 2015. I hope you will find the information provided here helpful and of interest.

If you would like to share Dentons' insights with friends or co-workers, please send their name, business position and e-mail address to: dentonstaxadvisory@dentons.com

Sincerely yours,



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# Contents


| | |
|---|---|
| The meaning of "fixed establishment" in the VAT Directive | 4 |
| Change of a tax ruling issued as a result of a final and non-appealable judgment | 6 |
| Loss from the transfer of time-barred claims | 8 |
| Tax base for civil law transactions tax charged on the establishment of a partnership limited by shares | 10 |

# The meaning of “fixed establishment” in the VAT Directive

## Ruling description

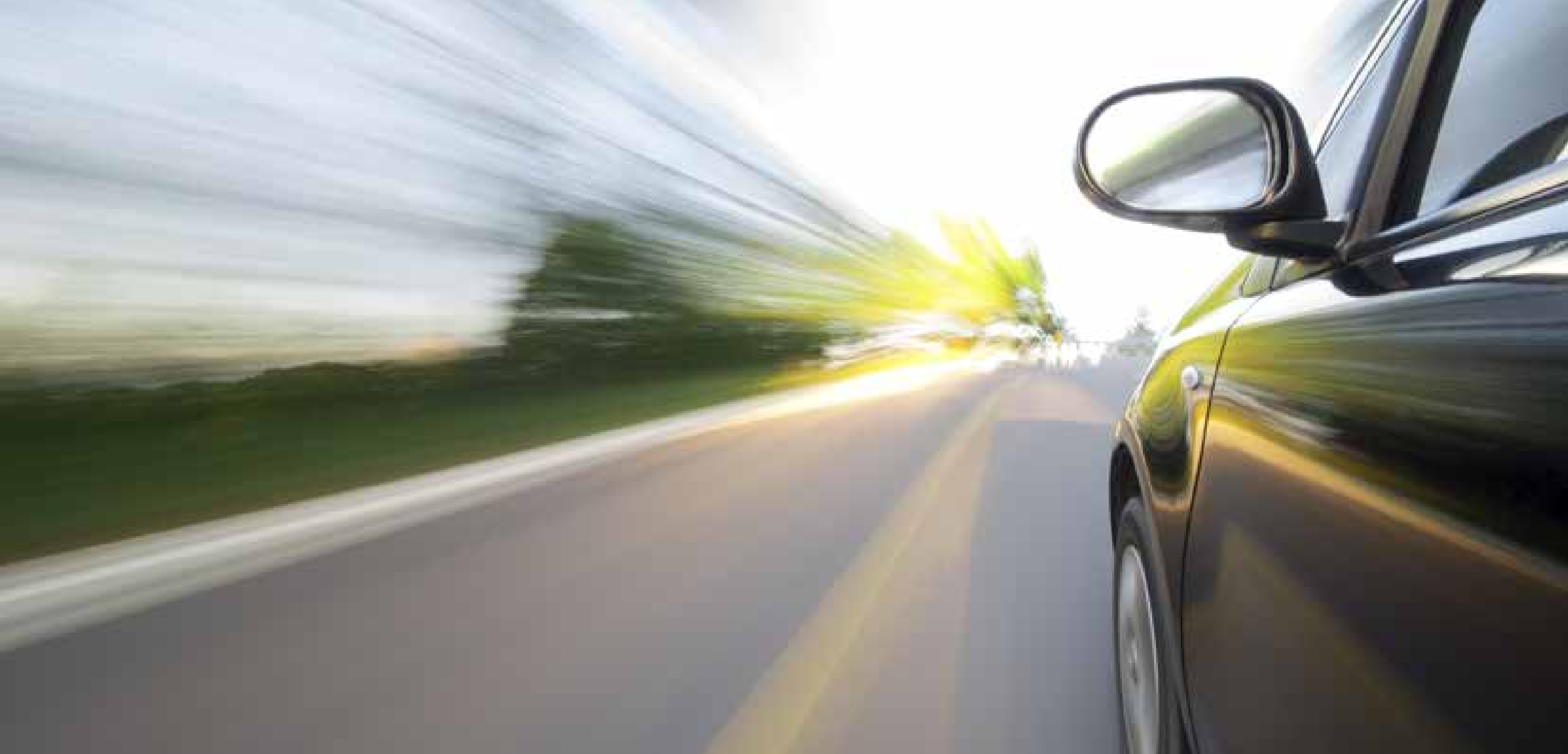
On September 25, 2015, the Supreme Administrative Court issued a judgment (case file no. I FSK 578/15), in which it addressed the notion of “fixed establishment” for the purposes of VAT and the abuse of rights in connection with VAT.

The Supreme Administrative Court ruling was issued in a case involving a Polish taxpayer, which was similar to a case resolved in 2014 by the Court of Justice of the European Union (ECJ) in the C-605/12 judgement. This is one of the first Polish court awards regarding the fixed establishment issued after the ECJ judgment.

In the case at hand, the Polish company signed a contract with a business partner from Cyprus, whereby the Company agreed to perform the whole package of services necessary for an e-commerce service to function (an internet auction service organized by the Cypriot company) targeted at Polish users. The Company submitted that the services provided to the Cypriot counterparty are subject to VAT taxation in the country where the service purchaser is seated, i.e. in Cyprus (this is in line with the basic rule for determining the place of the provision of services under Art. 28b of the VAT Act). Tax authorities ruled that the Polish business partner has a fixed establishment in Poland and that the services were therefore provided by the Polish company for the Polish fixed establishment. Consequently, the services provided by the Polish company ought to be subject to VAT taxation in Poland.

The Provincial Administrative Court agreed with the tax authority’s case. Moreover, the Supreme Administrative Court dismissed the last resort appeal filed by the Polish company.  The Court pointed out that although the business partner is registered in Cyprus, the entire business activity is conducted in Poland, considering that the service is to a large extent maintained and provided by the Polish company, and that it is targeted at Polish consumers.  For this reason, a Cypriot taxpayer has a fixed establishment in Poland and the services provided to the Cypriot taxpayer ought to be taxed in Poland.

In the judgment on appeal, the Supreme Administrative Court also touched upon the notion of an abuse of a right in connection with VAT. The Court noted that according



to a rights abuse test, if an artificial structure has not been developed due to economic or business needs and the prevalent purpose of this structure is to pay a substantially smaller tax or not to pay tax at all, a taxpayer must not benefit from the solutions/benefits available under the VAT Directive. The Supreme Administrative Court announced that in the written statement of grounds it will address in more detail the question whether the law has been abused in the case at issue.

## Comment

The judgment at issue is of crucial importance for taxpayers, who – in collaboration with foreign contractors – provide or receive services to/from these contractors, especially in outsourcing models. In light of the judgment, Polish taxpayers acquiring services from foreign contractors (especially in the outsourcing model) may be found to perform their activities in the contractor's country of residence through a fixed establishment, and therefore may be subject to VAT in this country. Conversely, for taxpayers providing services to foreign contractors (as is the case in the lawsuit at stake), they run the risk of being deemed to provide services for the benefit of the contractors' fixed establishment in Poland. In such a situation, the tax authorities may make an assessment of overdue VAT and charge default interest. Special attention needs to be paid by e-commerce and electronic businesses where no substantial human or technical resources need to be involved. In those sectors, tax authorities will find it easier to deem that the contractor's assets became an overseas fixed establishment of these businesses. When assessing this risk, it will also be necessary to take into account the Supreme Administrative Court's conclusions regarding right abuse tests in light of VAT regulations.

Additionally, we note that the Supreme Administrative Court's judgment does not relate to one of the most essential issues as regards the interpretation of the term "fixed establishment". It was pointed out in ECJ judicature that a fixed establishment may be created by human and technical resources of a different taxpayer, but only if the 'first taxable person' has a comparable degree of control over these resources as it has over its own resources. This premise was not discussed in detail (at least in the oral discussion of the statement of grounds), and therefore it will be necessary to verify this issue once again after the written version of the statement of grounds is published.

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# Change of a tax ruling issued as a result of a final and non-appealable judgment

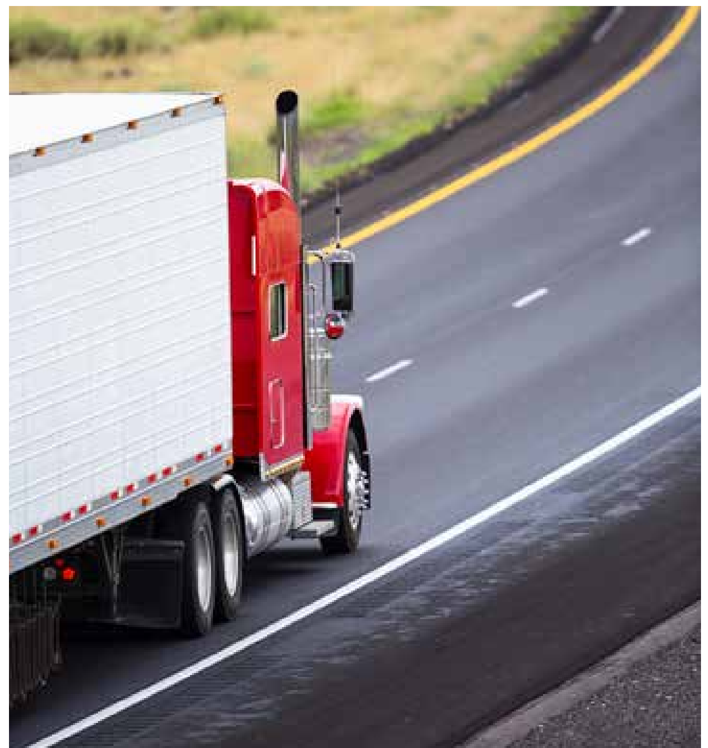
## Ruling description

As arises from the judgment of the Supreme Administrative Court of 25 September 2015 (case no. I FSK 563/14), the Minister of Finance may change a tax ruling issued as a result of a final and non-appealable judgment of an administrative court.

A company asked for a tax ruling in a case concerning VAT. In the application it requested the authority to confirm the tax rate applicable to the supply of a medical device together with its installation and adaptation works. According to the applicant, both the supply of medical devices and the related assembly and adaptation works should be, as a package of services, subject to the preferential rate of 7%.

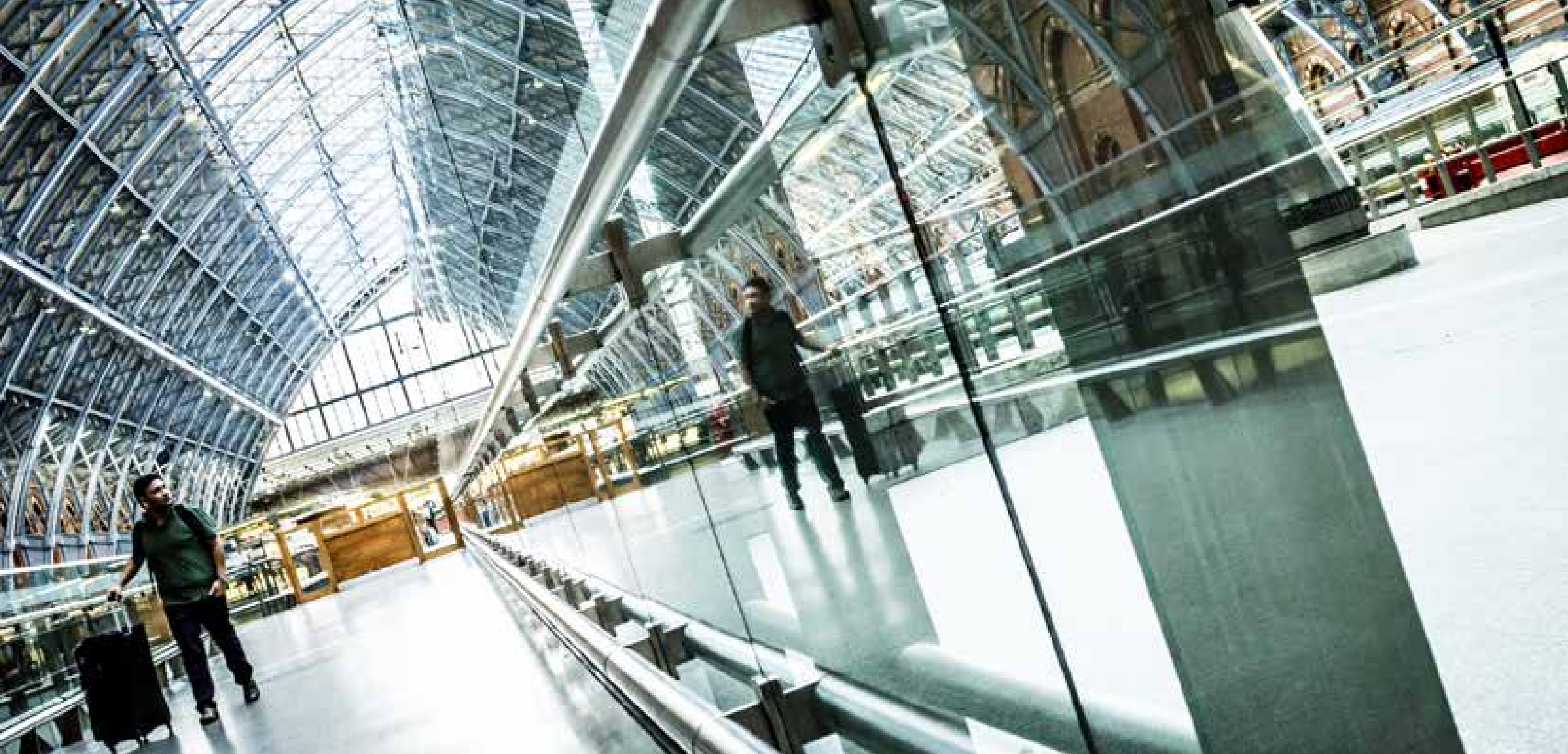
The Head of the Tax Chamber in Warsaw, in his tax ruling of 14 July 2009, considered that the company's position is incorrect. According to the authority, though the performance of construction and assembly works is related to the supply of a medical device and is intended to ensure correct and safe work of the product, it may not be assumed that such services constitute an element of a comprehensive performance, namely the supply of a medical device.

The Provincial Administrative Court in Warsaw reversed the tax ruling on appeal and acceded to the Company's position. As a result of the incorrect specification of the grounds of the cassation, the Supreme Administrative Court dismissed the authority's cassation appeal. As a result of a final and non-appealable judgment of the



Provincial Administrative Court, in 2010 the Minister of Finance issued a tax ruling in which it considered the Company's position correct.

In the same period the judicial practice of administrative courts became more consistent, as based on the ECJ case law the courts differentiated between adaptation works subject to the base VAT rate and the supply of a medical device subject to a preferential rate.



Then in 2012 the Minister issued a ruling amending the abovementioned tax ruling, in which it stated that the Company's position is incorrect. The Provincial Administrative Court reversed the change of the ruling and pointed out that in a situation where a taxpayer obtained a tax ruling confirming its position and the ruling was issued in performance of an administrative court judgment, the Minister of Finance, acting within the scope of its competences set forth in Art. 14e § 1 of the Tax Ordinance, could not change that ruling ex officio. According to the court, pursuant to Art. 170 of the Law of Proceedings before Administrative Courts, the Minister was bound by the final and non-appealable judgment. It means that a tax ruling of 2010 confirming the Company's position presented in the application for the tax ruling and implementing the guidelines contained in the final and non-appealable judgment issued in the case, is valid in the system of legal transactions.

However, the Supreme Administrative Court reversed the judgment of the Provincial Administrative Court, as the Tax Ordinance does not provide for any possibility to change a tax ruling issued as a result of a court judgment. Provisions of the Law of Proceedings before Administrative Courts on the binding force of an administrative court judgment are not applicable to this case, as a changed tax ruling is a new case. Additionally, the trial court did not examine material prerequisites of the change of the tax ruling in this case, though a new judicial practice has already been established.

## Comment

The scopes of application of provisions of Art. 14e and 170 of the Law of Proceedings before Administrative Courts are different and concern different situations. No possibility to change a tax ruling issued as a result of a final and non-appealable administrative court judgment would lead to a breach of a constitutional principle of equal justice under law. If a judicial practice different from the one arising from a tax ruling which is not subject to a change is established, a taxpayer would actually enjoy a tax privilege not expressly envisaged in tax law.

The discussed judgment is a precedent one, as courts had never before dealt with this issue. It follows from the judgment that the fact of issuance of a judgment concerning a tax ruling does not exclude the possibility of its amendment. However, the amendment would still be subject to court inspection in terms of existence of certain prerequisites (in particular taking into consideration the judicial practice of courts, the Constitutional Tribunal or the ECJ). Additionally, until a tax ruling is changed, a taxpayer may adhere to it and enjoy protection it provides. Therefore, immediate adherence upon the receipt of the ruling is worth considering.

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# Loss from the transfer of time-barred claims

## Ruling description

The Director of the Tax Chamber in Katowice bucked the now prevailing trend in court rulings and found in his tax ruling dated 1 September 2015 (ref. no. IBPB-1-2/4510-184/15/MS) that losses from sale of time-barred claims against consideration may not be deemed tax-deductible costs, even when the claims at issue had previously been recognized as revenues due.

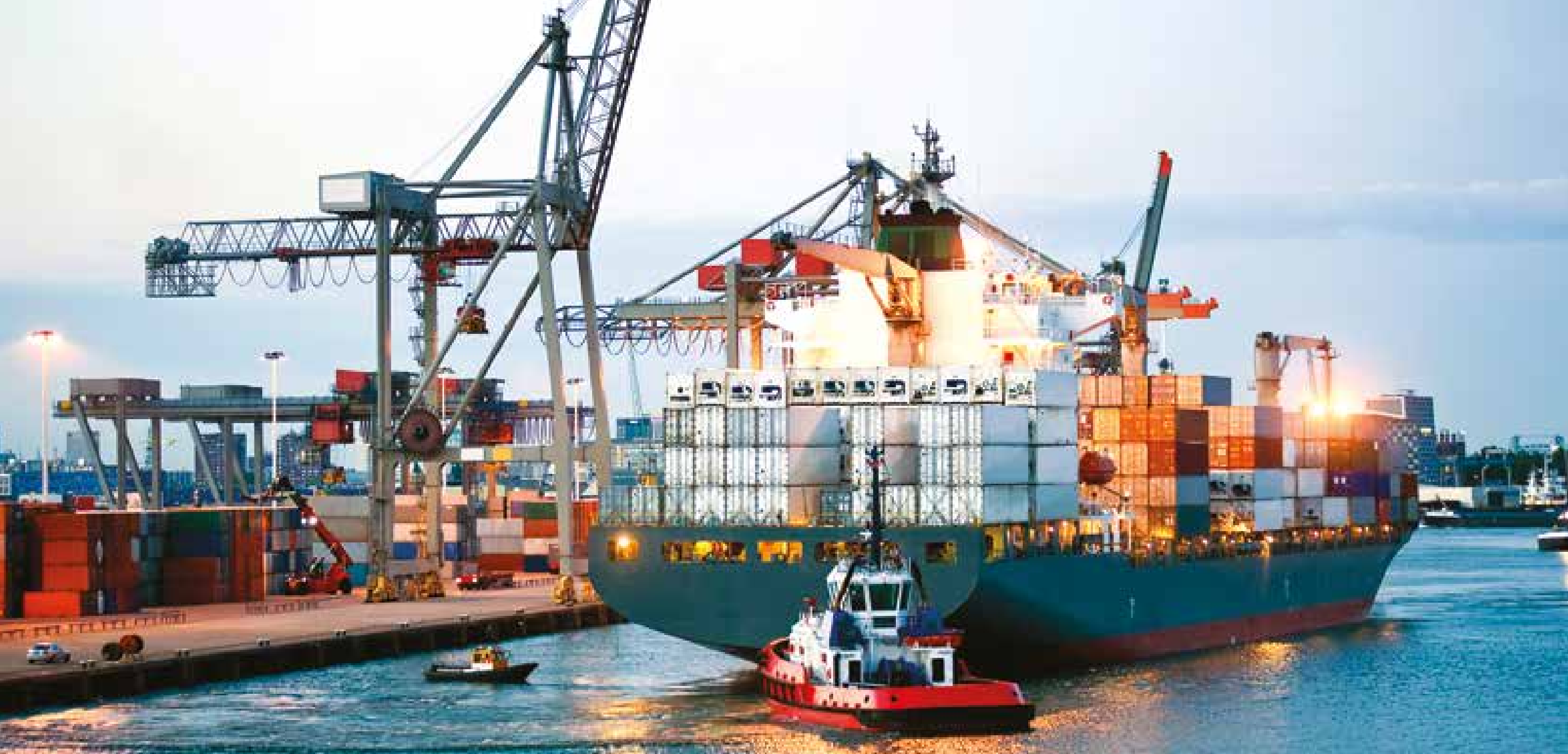
The CIT Act both prohibits the classification of time-barred claims as tax-deductible costs (Article 16(1)(20)) and allows tax-deductible costs to include losses resulting from the transfer—against consideration—of claims previously recognized as revenues due (Article 16(1)(39)).

In the case at issue a taxpayer transferred a package of claims, previously classified by it as revenues due, against consideration, to an affiliate whose business activities include debt recovery. The claims were sold at a much lower price than their nominal value, which resulted in the taxpayer incurring a loss on this sale transaction. Some of the claims were already time-barred on the date of this transaction. The taxpayer applied for a tax ruling to confirm that the loss on the sale of the time-barred claims is classifiable as tax-deductible costs. The tax authority disagreed, however, assuming that the mentioned Article 16(1)(20) of the CIT Act must be applied together with Article 16(1)(39) of this Act. The tax authority thus held that although the general rule set out in Article 16(1)(39) of the CIT Act is that losses from a transfer, for consideration, of claims recognized as revenues due may, in principle, be classified as tax-deductible costs, it follows from Article 16(1)(20) of the CIT Act that if the claims had been time-barred, these losses may no longer be viewed as tax-deductible costs. The tax authorities also argued that the ban provided for in Article 16(1)(20) of the CIT Act is to be interpreted in terms of a penalty for dilatory taxpayers letting their claims become time-barred. In other words, the tax authority believed the taxpayer cannot seek the tax benefits that go with recognizing a loss from a transfer, against consideration, of a claim which, due to the taxpayer's negligence, is no longer subject to enforcement, and therefore represents a loss.

## Comment

The tax ruling reviewed here is in line with the stance being taken by fiscal authorities, consistently disadvantageous to the taxpayer (cf. e.g. the tax ruling issued by the director of the Tax Chamber in Poznań on 29 April 2014, ref. no. ILPB3/423-40/14-2/KS; a similar position was also presented in previous years).

This position of the fiscal authorities is, however, inconsistent with the position the courts have taken until now (cf. e.g. the judgment of the Provincial Administrative Court in Wrocław of 8 January 2015, case file no. I SA/Wr 2017/14, the judgment of the Provincial Administrative Court in Warsaw of 28 August 2012, case file no. III Sa/Wa 2835/11, or, with some reservations, the judgment of the Provincial Administrative Court in Warsaw of 27 January 2014, case file no. III SA/Wa 1703/13) whereby losses on the sale of time-barred claims against consideration may be deemed tax-deductible costs provided the claims had



previously been recognized as revenues due. The courts are of the view that the scopes of application of the two regulations mentioned above are distinct: Article 16(1)(20) of the CIT Act prohibits the classification of claims as tax-deductible costs for the sole reason of the claims having become time-barred, while 16(1)(39) of the CIT Act is an entirely separate regulation governing transfers of claims previously recognized as revenues due for consideration. The two regulations cannot, therefore, apply jointly and the only regulation that applies to a transfer of claims for consideration is Article 16(1)(39) of the CIT Act which refers precisely to this kind of transaction. The courts also point out that the said Article 16(1)(39) of the CIT Act applies equally to time-barred claims and those that are yet to become time-barred. Moreover, according to the courts, given the unequivocal wording of Article 16(1)(39) of the CIT Act and the absence of any reasonable axiological reasons to challenge it, there are no grounds for any additional interpretations aimed at modifying how the literal wording of this regulation is construed.

In an important development, the Supreme Administrative Court recently reiterated the above position in a judgment of 5 February 2015 (case file no. II FSK 3113/12). As can be seen from the tax ruling reviewed here, this judgment is yet to have a practical impact on the pronouncements of the fiscal authorities.

Taxpayers transferring their time-barred claims against consideration must therefore reckon with the risk that tax authorities will challenge the classification of the losses incurred as a result of such transfer in the tax-deductible costs category. In order to minimize this risk, taxpayers would be well advised to consider applying for a tax ruling, especially if the transaction involves substantial amounts of money or if it is one of many of its kind. If the tax authority comes back with a negative opinion, the taxpayer will have an opportunity to appeal the ruling to a court and will quite probably win the case. Taxpayers which had already effected transactions of this kind must be aware of the risks they are facing when accounting for the losses they incurred. These risks may only be mitigated by adopting an appropriate litigation strategy. In any case, it will be interesting to monitor future developments to see if the cited Supreme Administrative Court judgment eventually prompts the tax authorities to abandon their rigidly held views that are disadvantageous to taxpayers.

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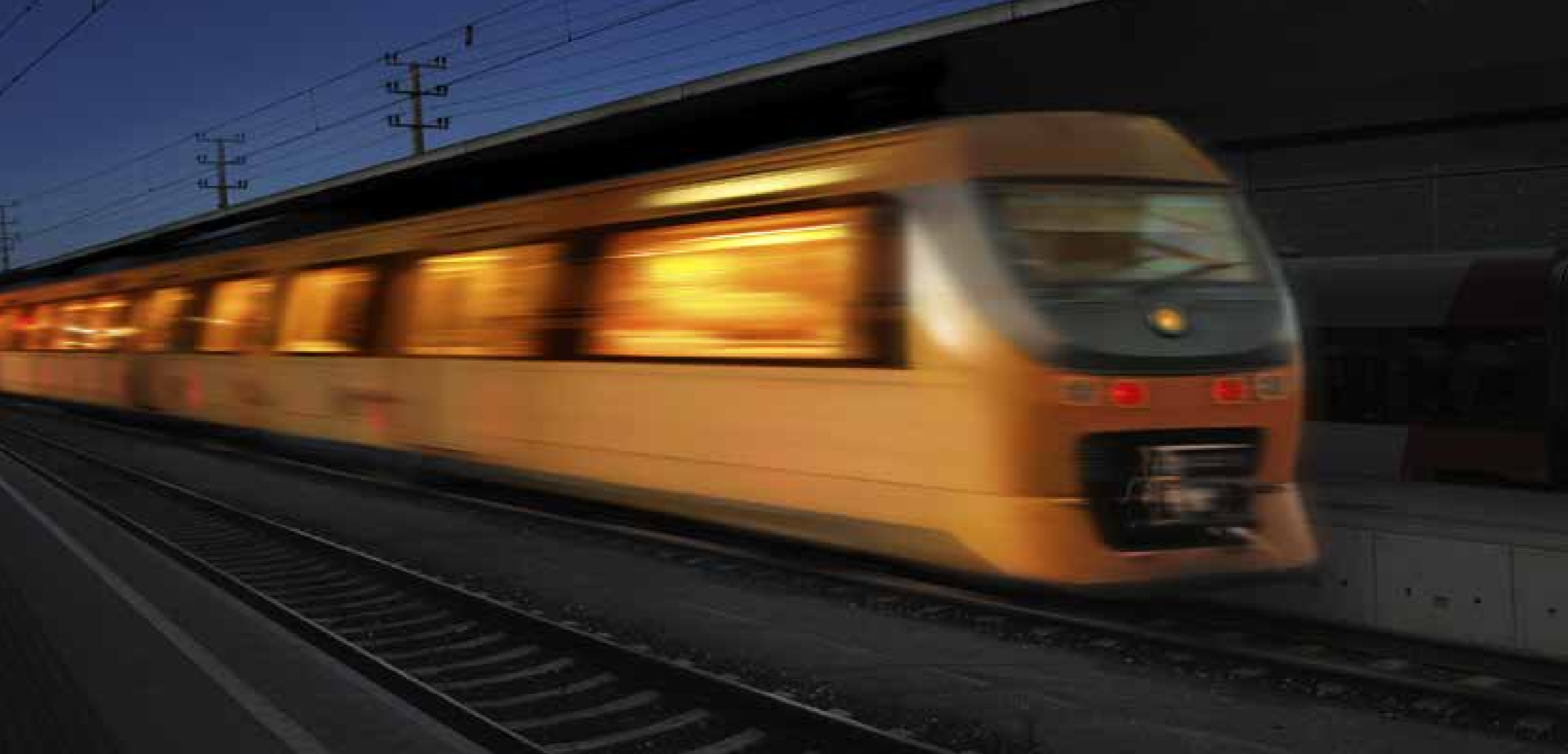
# Tax base for civil law transactions tax charged on the establishment of a partnership limited by shares

## Ruling description

The Provincial Administrative Court in Gliwice issued a judgment on 28 September 2015 (case no. I SA/GL 583/15) in which it described the methodology of calculating the basis of assessment for the tax on civil law transactions (TCLT) to be levied on the founding of a partnership limited by shares (PLS).

A PLS (in organization) was established by virtue of a notarial deed in which the partnership's share capital was put at PLN 50,000.00, this being just part of the monetary contribution made at the time of the founding of the PLS. The rest of the monetary contribution (over and above the nominal value of shares) was allocated to the PLS's surplus capital. The notary, acting in its capacity as payer, collected the tax on civil law transaction calculated for the aggregate amount contributed to the share and surplus capital.

The PLS applied for a tax ruling to clarify whether the amount subject to tax on civil law transactions ought to include also the contributions exceeding the share capital. The position of the PLS was that TCLT ought to be levied in connection with the founding of the PLS only on the amount of the share capital contributed on the date of the partnership's founding while the additional amount contributed by a shareholder and allocated to the PLS's



surplus capital should be excluded from the basis of assessment for the TCLT.

The Director of the Tax Chamber in Katowice disagreed with the PLS, emphasizing that while, as can be seen from the Commercial Company Code, the PLS is a partnership with many elements of a capital company (including the share capital), this does not mean that it must be treated differently from other partnerships on the grounds of the Act on Tax on Civil Law Transactions. The Director argued that upon the execution of the deed establishing the PLS, the basis of assessment for the tax at issue ought to include the sum total of the contributions being made to it (including those made in addition to the share capital), as would be the case with every other type of partnership.

The Provincial Administrative Court in Gliwice set aside the appealed tax ruling, explaining that while the tax authority correctly assumed that on the grounds of Polish law a PLS is a partnership, the court is bound first and foremost by EU laws, including the Capital Duty Directive (2008/7/EC) in which organizations like PLSs are classified as capital companies. Therefore, when determining the basis of assessment for the TCLT, the PLS must be treated as a capital company. Accordingly, the monetary contribution exceeding the PLS's share capital is not subject to TCLT.

## Comment

This judgment is another in a series of rulings in favor of TCLT payers operating as PLSs. It must be applauded as being in line with the currently prevailing trend in administrative court rulings, resulting from, among other things, the judgment recently handed down by the EU Court of Justice in the Drukarnia Mulitipress case (C-357/13) in which the Court explicitly stated that in the sense of the Capital Duty Directive (with the TCLT being in fact a form of capital duty), Polish PLSs must be deemed capital companies. As a result, the basis of assessment for the TCLT to be levied in connection with the formation of a PLS must be determined as in the case of any other capital company and not as for a partnership.

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