

Provincial Administrative Court denies protection of individual tax ruling for real estate transaction

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In Brief

The change in the approach of the tax authorities in relation to the VAT classification of real estate transactions has recently caused uncertainty in the Polish real estate market. In the tax authorities' opinion the sale of leased commercial properties, which has been previously usually seen as sale of assets on a piecemeal basis, should be classified as the sale of a going concern (an enterprise or an organized part thereof). Thus, the tax authorities have recently challenged VAT refunds on completed transactions. A recently issued judgement of the Provincial Administrative Court in Szczecin seems to share the new approach of tax authorities. **What is worse, protection under an individual tax ruling has been denied because of insufficient background information. It is advisable to review the actual facts and circumstances of the past transactions in comparison to the proposed facts and circumstances described in the ruling request to assess the risk and the possibility of mitigating it.**

Details

The Provincial Administrative Court in Szczecin (I SA/Sz 901/16) ruled that the sale of a shopping centre should be classified as a sale of an organized part of an enterprise (a "going concern") and denied recovery of input VAT to the buyer.

The transaction was performed between related parties. Post-closing, the operation and management of the shopping centre remained substantially unchanged.

Recoverability of input VAT by the buyer was confirmed in advance by a ruling of the Ministry of Finance. It appears however that the description of background of the transaction presented in the ruling application lacked a number of facts.

Classification of the object of transaction as an organized part of an enterprise

In the court's view, the conditions for classifying the deal as the sale of a going concern had been fulfilled. It concluded that components of the transaction have been

organisationally and financially separated within the existing enterprise and constituted a set of functionally related tangible and intangible components intended to perform specific business tasks.

In the court's view, comprehensive provisions included in the SPA relating to lease agreements indicate that the transfer of these agreements was crucial for the parties and allowed uninterrupted continuation of lease agreements.

The court stated also that the transaction included elements which could constitute an independent enterprise performing business tasks by itself. The court underlined that agreements enabling continuing of business activity of the seller (such as the management agreement, the accounting agreement) have been concluded by the purchaser with the same entities, being related parties to both seller and the purchaser, whilst the director of the shopping centre was intended to be retained regardless of the transaction.

Denial of protection under individual tax ruling

The court denied the protective power of an individual tax ruling issued to the company, as in its view the actual transaction had not corresponded to the conditions described in the tax ruling request. The court stated that the company had omitted several key circumstances. In particular, the tax ruling request had not contained information that the buyer is a special purpose vehicle and the seller and the purchaser are related parties. The court considered this circumstance as particularly important, because as a result of which in the court's opinion the purchaser was able to use the name of the shopping centre (which is owned by the parent company), as well as accounting and management services provided by the same entities. Moreover, the company had not mentioned the fact that the shopping centre has internal procedures regulating the operations of the shopping centre and property's budget.

Furthermore the court reasoned that the company had omitted information that the purchaser had intended to immediately conclude service agreements with the same entities and as a result activities related to operation of the shopping centre are performed by the same individuals as before the transaction.

We understand that the taxpayer has appealed against the above judgment to the Supreme Administrative Court, whose verdict may be expected in 2 years.

What does it mean for me?

For a few months now, the tax authorities have been aggressively challenging the classification of the sale of commercial real properties as VATable transactions and denying the refund of VAT charged on the sale. The approach of the court may strengthen the resolve of the tax authorities' practice in classifying the real estate transactions as sales of a going concern.

A particular concern from the market perspective is that the court denied protection of the individual tax ruling. In this case the background provided by the buyer in the ruling according to the court lacked the number of important facts. On the other hand, some of the items omitted from the ruling request which led the court to disregard the ruling, was also not – according to market standards - included in tax ruling requests filed in relation to similar transactions.

In this context, the judgment may encourage tax audit authorities to challenge VAT taxation of past

real estate transactions, where VAT has already been refunded. It cannot be ruled out that this situation may occur even if the taxpayer has obtained a positive individual tax ruling and received the VAT refund. Consequently, it is advisable to review the actual facts and circumstances of past transactions against the description provided in the ruling request to assess the potential risk and possibilities to mitigate it. This should be done with respect to all transactions where a VAT refund is not yet covered by statute of limitations, i.e. generally transactions since December 2011.

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