Real Estate Tax Services News

Keeping you informed

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Taxation of the real estate investments in Poland - key updates

In brief

On 28th June 2022 a draft law amending the Corporate Income Tax Act and certain other legal acts was published by the Polish government. The tax changes stipulated in the draft law mostly concern corporate income tax (CIT) and a number of them are likely to have a significant, direct impact on the taxation of real estate investments in Poland. Below we provide the outline of the key proposed changes in the CIT law.

The draft law is currently at the government and public consultation stage and the government plans to adopt the draft law in the third quarter of 2022. Further developments in this respect should be monitored.

Changes in diverted profits tax

As of January 2022, a so-called "diverted profits tax" has been introduced. This tax is imposed @19% on “diverted profits” understood as costs (such as intangible services, royalties, debt financing cost or payments for transfer of functions, assets or risks) incurred - directly or indirectly - for the benefit of related entities (provided that certain conditions are met). Payments made directly/indirectly to entities subject to tax on their worldwide income in the European Union (EU) or European Economic Area (EEA) and conducting genuine, material business activity in these countries should be excluded from diverted profits tax.

Since there are a lot of unclarities regarding the interpretation of the currently binding provisions regarding diverted profits tax, the Ministry of Finance considers introducing some changes. Due to the substantial number of the changes, below we outline the ones which - in our view - may be crucial for real estate structures:

- The diverted profits tax is to apply only to **expenses that qualify as tax-deductible costs**. Note that the currently binding wording of the regulations (i.e. the one prior to the considered changes) does not contain clear provisions in this respect - thus there is a doubt whether diverted profit tax applies only to expenses qualifying as tax deductible costs, or also to the non-tax-deductible expenses (while the latter would be unfavourable for the taxpayers and against the common-sense approach). Thus, the proposed change is beneficial for the taxpayers.
- The diverted profits tax is to apply only if the **related entity**, for whose benefit the costs are incurred, **does not have its registered office or management in the territory of Poland** (with one exception relating to the payments to tax transparent entities - which are omitted in this alert). However, in practice, this regulation will cover most of the real estate structures.
- According to the current wording of the diverted profit tax provisions, this tax should be applied to expenses incurred directly or indirectly to related parties. As a result of new wording of the regulations, diverted profits tax will be - as a rule - applied if the expense is **directly incurred for the benefit of a related party**. However, at the same time, draft law includes the new provisions, according to which (1) even if a direct recipient, does not meet the conditions for the application of diverted profits tax, but (2) he transfers the obtained payment to another entity - it is necessary to analyse whether the “another entity” mentioned in point (2) meets the conditions for the diverted profits tax, hence the diverted profit tax is due anyway. Separate provisions are proposed with respect to the payments transferred to the tax transparent entities (which are omitted in this alert).
- As regards the **exclusion** form diverted profits tax for the payments to entities **subject to tax on worldwide income and conducting genuine, material business activities** in the EU / EEA, the provisions **are not planned to be changed**. However, due to the planned introduction of the changes mentioned in the bullet above, it seems that under the proposed provisions the taxpayers should analyse the situation only one level above the direct payment recipient. This may lead to a situation where, depending on the given structure, different tax consequences may arise. Also, it needs to be analysed whether this exclusion may apply to investment funds which are tax residents in the EU / EEA, but benefit from general CIT exemptions (commonly present in the real estate structures).
- The diverted profits tax is to apply only if the foreign related entity is taxed at an **effective tax rate of less than 14.25%** on a **specific qualified payment** obtained from a Polish taxpayer - while under the currently binding regulations the test is applied to the total tax result of the foreign related entity. The methodology of calculating the effective tax rate under the proposed regulations is not fully clear and requires further clarifications.
- Clarification that in order to be caught by diverted profit tax, at least 50% of the taxable revenues of the related entity being the payment recipient must be revenues from the “qualifying” costs for diverted profit tax purposes, **obtained from the Polish taxpayer or its related companies also being Polish taxpayers**. Note that the current wording of these provisions did not refer to the Polish entities only. After the change, if the foreign recipient will be an entity who has a wide portfolio of foreign companies underneath and will obtain revenues from these companies, this criterion will likely not be met, thus diverted profit taxation will not apply (this however should be assessed on a case by case basis). For the holding companies keeping only the Polish investments, the change should have no material impact.
- Other changes regarding diverted profit tax, which are not commented here, as they are not crucial for real estate structures. Should you however wish to discuss them in detail, please kindly let us know.

Formally, all above changes are to be applicable since 2023. However, in the explanatory memorandum to the bill it is indicated that some of the changes are clarifying in nature - which means that they may potentially be taken into account when interpreting the currently binding rules and settling the tax for 2022.

Changes in so-called general minimum CIT

As of January 2022, the new "general minimum CIT" has been introduced (next to the minimum CIT on commercially leased buildings - which is a different type of tax). According to the currently binding provisions, general minimum CIT is applicable to all taxpayers declaring tax losses or negligible taxable income (<1% of the taxable revenue) from other operational activity basket - subject to a reservation that the tax depreciation write-offs should be disregarded for the purpose of determining the above loss / share of income in the revenue. The tax rate is 10% of the tax base calculated in accordance with specific rules stipulated in the CIT law. Additionally, certain exclusions from general minimum CIT apply - and relate to the taxpayers meeting specific criteria (e.g. taxpayers suffering from substantial revenue decrease, taxpayers during the first 3 years of operations etc.).

Under the draft law it is planned to **suspend the application of the general minimum tax for a period of 1 year**, i.e. from 1 January 2022 to 31 December 2022 - so that it will apply starting from 2023. In the meantime, the Ministry of Finance plans to **change the regulations** - and the proposed changes include i.a.:

- **Increase of the threshold profitability ratio from 1% to 2%.** Note that changing the ratio is not beneficial for the taxpayers - as it is intended to lead to potential levying general minimum CIT on the taxpayers with the profitability between 1 and 2%.
- Changes in the **methodology of calculation of the tax loss / the profitability threshold**. The impact of this change should be assessed on a case-by-case basis.
- Extension of the catalogue of **exclusions** from this tax, for e.g. the taxpayers whose **profitability ratio in 1 of the last 3 tax years preceding a given tax year was above 2%**. This means that even if a taxpayer in the current tax year incurs a tax loss or its revenue/income ratio is above 2%, he may not be taxed with general minimum CIT if in at least 1 of the previous 3 tax years he had the ratio exceeding 2%. This should lead to elimination of the situations where the taxpayer would fall under the general minimum CIT “by accident”, due to recording the tax loss / low tax profitability in one single tax year only.
- Changes in the calculation of the **tax basis** for general minimum CIT.

Removal of 'hidden dividend' regulation

The 'hidden dividend' regulations - i.e. the provisions:

- intended to exclude from tax deductible costs so-called “hidden dividends”, i.e. certain payments made for the benefit of shareholder (or entities related to shareholder/taxpayer) which could be seen as aimed at replacing dividends;
- which were to come into force on 1st January 2023;

are planned to be fully **revoked**. This change is beneficial for the taxpayers.

Other changes

Other changes considered under the draft law include i.a.:

- “Compliance” changes regarding filing the so-called WHT remitter’s statement - which, under the WHT collect and refund mechanism, is one of the documents allowing the WHT remitter to apply WHT exemptions/reduced rates in case of payments subject to WHT with the aggregate value exceeding PLN 2m.
- Change of the transfer pricing rules regarding direct/indirect transactions with tax havens.

Next steps

As mentioned above, the final shape of the changes in the Polish Deal are currently being worked-out. Thus, in case you e.g.:

- make payments which may be covered by diverted profit tax or
- may potentially fall under general minimum CIT;

it is highly recommended to monitor further developments in this respect. Should you wish to discuss with us the practical impact of the changes on your structure, please kindly contact us.

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