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Planned amendments to the Corporate Income Tax Act as of 1 January 2017

The Ministry of Finance has published draft amendments to the Personal Income Tax Act and the Corporate Income Tax Act dated 22 February 2016 (hereinafter: the “draft”). The amended provisions, apart from certain exceptions, are expected to enter into force as of 1 January 2017.

Below we present the most important amendments to the Corporate Income Tax Act (hereinafter: the “CIT Act”)

1) Changes in taxation of in-kind contributions allocated to share premium

According to the draft amendments to the CIT Act, the taxpayer's taxable gain resulting from an in-kind contribution in a form other than a business or its organised part would be determined in the amount of such contribution specified in the statute, articles of association or other document, instead of the nominal value of shares acquired in exchange for an in-kind contribution as it is currently regulated under the CIT provisions.

If the value of in-kind contribution differs from its market value, the taxable gain will be determined as the market value of such a contribution.

The provisions determining tax deductible costs at the date of acquisition of shares in exchange for an in-kind contribution (in a form other than a business or its organised part) as well as provisions governing tax deductible costs on the disposal of these shares,

have been amended accordingly and subjected to transitional rules.

Moreover, in accordance with the planned amendments, the existing limitation in tax deductibility of depreciation write-offs on the value of an in-kind contribution allocated to share premium would be repealed. As per the interim provisions, this limitation would however still apply to taxpayers to which the in-kind contributions will have been made before the date of entry into force of this amendment.

2) Existence of valid business reasons as a condition of tax neutrality of a share-for-share exchange transaction

Pursuant to the draft amendments to the CIT Act, in order to benefit from the preferential taxation applicable to share-for-share exchange transactions, valid business reasons should exist.

The draft bill introduces also the presumption according to which if a merger, demerger or a share-for-share exchange was not carried out for valid business reasons it shall be deemed as executed with the main objective (or one of the main objectives) of avoiding or evading taxation.

3) Amendments to the withholding tax exemption on interest and royalties (“beneficial owner” status)

According to the explanatory notes to the draft amendments to the CIT Act in the current wording of Article 21 clause 3 of the CIT Act the legislator uses the term “*recipient*

of payment” which may raise interpretational doubts, despite the existing distinction between the term “*recipient of payment*” and “*entity receiving income*”. Therefore, it is proposed to clarify this provision and explicitly determine that the entity receiving royalties and interest must be the beneficial owner of those royalties and interest in order to benefit from the withholding tax exemption based on Article 21 clause 3 of the CIT Act.

4) Introduction of the definition of income earned within the territory of the Republic of Poland for the purpose of determining the limited tax liability for non-Polish residents

According to the explanatory notes to the draft amendments to the CIT Act, the lack of the definition of the term “*income earned within the territory of the Republic of Poland*” (or even lack of a catalogue of examples of types of such income) may result in taxable income received by non-Polish tax not being recognized, e.g. in the case of disposal of shares/interests in a Polish company (or partnership) whose assets consist primarily of real estate, despite the fact that the right for taxation of such gain is granted to the Republic of Poland under the given double tax treaty.

The draft provides for an open catalogue of example situations in which the income of a non-resident is explicitly deemed as earned “within the territory of the Republic of Poland” for the purpose of determining the limited tax liability in Poland.

**5) Clarification of the term
“cancellation of shares”
for the purpose of a demerger**

Pursuant to the draft amendments to the CIT Act, the term “*cancellation of shares*” (as stated in Article 16 clause 1 point 8c letter c and in Article 10 clause 1 point 6 of the CIT Act) would also refer to a reduction of nominal value of shares.

The current wording of Article 16 clause 1 point 8c letter c of the CIT Act may lead to the conclusion that when as a result of the demerger through spin-off there would be no reduction in the number of shares held by the shareholder in the demerged company, but their nominal value would be reduced, then upon the disposal of such a company’s shares the amount of expenses incurred to purchase of these shares would constitute tax deductible costs in full.

6) Introduction of reduced 15 per cent CIT rate for so-called “*small*” taxpayers and taxpayers starting business activity in their first tax year

The presented draft proposes to lower the CIT rate from 19 to 15 per cent for so called “*small*” taxpayers, i.e. entities whose sales revenue (including output VAT) for the previous tax year did not exceed the equivalent in PLN of EUR 1,200,000 and the taxpayers starting business activity - in their first tax year.

According to the draft amendment, the 15 per cent CIT rate would not apply in case of taxpayers starting their business activity if this would be established as a result of one of the restructuring operations indicated in the proposed regulation. Those taxpayers will have the possibility to apply the 15 per cent CIT rate – only starting from their third tax year providing that in this tax year they will retain the “*small*” taxpayer status within the meaning of Article 4a point 10 of the CIT Act.

We would recommend that any planned transactions are analyzed taking into account the proposed amendments.

We would also like to draw your attention to the fact that the wording of the amended provisions may give some additional arguments in disputes with the tax authorities under the currently binding CIT provisions.

Please contact us if you would like to obtain more information on the draft amendments or discuss their impact on the obligations of your company.

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