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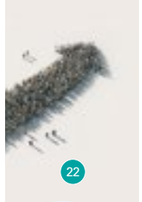

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RESEARCH AND DEVELOPMENT - NEW PERSPECTIVES FOR ENTREPRENEURS

Kiejstut Żagun and Bartosz Igielski in conversation with the editorial staff of the 'Turning Point' magazine. They talk about the new tax incentive for R&D and opportunities for entrepreneurs it entails.

Turning Point TP >: A new R&D tax relief is in force since 2016. What benefits does it provide entrepreneurs with?

KIEJSTUT ŻAGUN (KŻ):
R&D relief is an instrument used in numerous countries to encourage entrepreneurs to conduct research and development. It reduces income tax. Resources obtained in this manner can be used by entrepreneurs as they wish, including when they need to employ engineers and finance additional projects.

TP > So the more we conduct research and development work, the smaller the tax we are obliged to pay?

KŻ > Yes, the deduction allows you to deduct R&D costs with an additional bonus (calculated as a percentage) in the tax calculation. For example, having annual PLN 1m wage costs dedicated to R&D projects, a company may deduct PLN 1.5m for the tax year 2017 in its tax calculations. In short: it can effectively reduce income tax by almost 10% of the cost of these wages..

BARTOSZ IGIELSKI (BI):
From 2018 on, the effective tax reduction is expected to increase significantly, translating into a tax advantage of 19% of eligible costs.

TP > Can the company that received cash grants also benefit from the new R&D relief?

BI > Yes. R&D grants can be combined with new R&D relief. In such case, the relief applies the cost that were not covered by the cash grant.

KŻ > The advantage of the relief is the fact that a company has to just carry out research and development and does not need to show their level of innovation. It covers all eligible R&D costs cumulatively in a given tax year, you can claim the relief retroactively by way of a correction of the tax declaration.

TP > The results of the study on the use of relief have been presented recently for entrepreneurs. What conclusions can be drawn from this study?

KŻ > The study was conducted among companies that carry out Research & Development. Only one in nine companies benefited from the R&D tax relief for 2016. This relatively low result shows that many companies are unaware of the relief or exhibit cautious approach to this instrument. In our opinion, this is a wrong approach because the relief is a purposefully introduced support instrument, aiming to help entrepreneurs in the R&D area. The relief is much more obtainable than a cash grant (eg. there is no application contest as in the case of applying for a grant).

TP > What is the reason for this low level of interest in taking advantage of the relief?

BI > According to the majority of respondents, they do not apply from the relief because of the uncertainty as

>> R&D grants can be combined with the new R&D relief. In such case, the relief applies to the cost that were not covered by the cash grant.

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A tax advisor, head of Grants&Inventives team and a member of KPMG's international R&D Incentives expert group. He has many years of experience in obtaining incentives and grants for entrepreneurs, especially in the area of R & D & I. In KPMG since 1998, has assisted companies in the processes related to the preparation of funding strategies, which translated into multi-million dollar support for the entities with which he cooperated.
He has experience in raising funds from the EU Structural Funds, national resources, EU initiatives and other sources of investment support, R & D, innovations and environmental protection.

» The announced changes are very advantageous for entrepreneurs planning to benefit from R&D relief. They implement most of the demands made by companies regarding the relief settlement in 2016.

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to whether a given activity qualifies as research and development. Moreover, respondents estimate the risk that a tax office would contest the calculation as high. Less common responses pointed to lack of knowledge about the existence of relief and too little benefits to be gained from this instrument. Such concerns can be remedied by mapping the company's activities eligible to R&D relief and by preparing an annual R&D report in the company.

TP › And how do entrepreneurs plan to use the funds obtained from R&D?

KŻ › Most entrepreneurs declare that they will use the funds raised for the implementation of further R&D projects. This is good news because it will increase R&D expenditure in the private sector, and this is the main goal of the relief. Respondents also pointed to the need to purchase R&D equipment and to employ additional research staff. All this demonstrates the desire to increase research potential in companies and points to the increased importance of such activity among other branches of an enterprises.

TP › Did the companies participating in the study report any problems that occurred when using the relief?

KŻ › They did. The vast majority of companies reported such problems, most pointed to the difficulty of classifying expenditure as costs eligible for relief. We often encounter this problem with our customers who are not fully aware of whether the costs involved may be eligible for relief and how, for example, to assign costs to a project. Some of the respondents also pointed to problems with keeping accounting records of eligible costs and identifying which projects and activities in the company qualify as R&D.

TP › Is it possible to say that the relief is already a complete, mature instrument?

BI › Certainly not. The relief has been in force since 2016, one amendment has already been introduced, increasing the deduction under the relief from 2017, and another major amendment is planned from 2018, which will introduce a number of important changes. The position of the tax authorities regarding the interpretation of the rules of relief is also slowly taking shape.

PZ: Can we say more about the planned changes?

BI › The most important one is the increase the additional deduction level to 100% for all businesses (regardless of size) and for all categories of eligible costs. So far, the additional deduction was 50% for SMEs and 30 to 50% for large companies. In addition, companies with the status of a R&D center, obtained under the Act on various forms of support for innovative activities, may count on an additional deduction of up to 150% and thus an increase in tax relief.

KŻ › The catalog of eligible costs will also be expanded and clarified – employees' salaries will be eligible for a relief in a portion proportional to the time the employee devotes to R&D (there are plans to remove the "employment for ..." clause, which causes differences in interpretations and problems in documentation of that condition by employers conducting R&D). The eligible cost will be the remuneration of natural persons involved in R&D activities under fee-for-task agreement or a contract for a specific task. The cost of qualified R&D equipment, which is not a fixed asset, will also be eligible. Until now, such equipment was not included in the eligible costs catalog.

TP › Will there be any other benefits for R&D centers resulting from the change of legislation in addition to the additional deduction?

KŻ › Yes, they will be able to use the extended the eligible costs catalog, which includes additionally depreciation of edifices, buildings and offices constituting separate property, used in R&D, as well as acquisition of expertise, opinion, consultancy and peer services, research, technical knowledge, patents and licenses for a protected invention from entities other than research facilities. In addition, a status of a R&D Center can be obtained by declaring revenues of as much as PLN 2.5m, with R&D services sales at 70% or revenues of more than PLN 5m, with sales of R&D services at 20%.

TP › Does the amendment provide any other changes?

BI › One of the major changes will be to allow R&D tax relief for taxpayers carrying out the so-called 'non-zone' activity in the SEZ (Special Economic Zones). There is also a plan in place to extend the tax exemption for companies whose sole business is to make financial investments due to the sale of shares of entities carrying out R&D and acquired in 2016-2023.

TP › How would you rate the planned changes?

BI › The announced changes are very advantageous for entrepreneurs planning to benefit from R&D relief. They implement most of the demands made by companies regarding the relief settlement in 2016. Of course, some things need to be improved, but we believe that it will happen sooner or later, given the increasing importance the ministries show towards facilitating R&D carried out by companies in Poland. Thanks to these changes, a larger group of companies will be able to take advantage of the reduction, and interest in this instrument will increase among companies that have not benefited from it yet. This will be possible due to increasing the deductible amount, introducing the possibility of using the relief provided by the companies operating in SEZs and removing the requirement of having "workers employed for R&D purposes" to be able to deduct their salaries.

KŻ › Also important is the amendment of the regulations concerning research and development centers. So far they have not been very popular among entrepreneurs – currently there are several dozen such facilities. If regulatory changes mentioned above are introduced, growth of R&D Centers number can also be expected, also due to the lowering of the turnover threshold from which such status can be obtained. The changes proposed by the government should be rated positively, with a sole reservation that they have not been implemented earlier, so that they could be used for 2016 or 2017. ■

NEW REGULATIONS FOR AUDIT COMMITTEES

On 21 June 2017, the Act of 11 May 2017 on statutory auditors, audit firms and public oversight came into force. It specifies, among others, new rules relating to establishing and operation of audit committees in public interest entities.

»

What entities are affected by the changes?

The Act of 11 May 2017 on statutory auditors, audit firms and public oversight (Journal of Laws of 6 June 2017, item 1089, hereinafter referred to as the "Act") expands the catalogue of entities constituting public interest entities ("PIE"). However, the changes introduced under the Act with reference to the rules for establishing and operating audit committees will affect not only the entities that have been included in the PIE catalogue, but also entities which, according to the existing regulations, have already been on the PIE list. This particularly applies to entities where audit committees could be entrusted with the duties of the supervisory board and those that have not yet had to set up audit committees or entrust a supervisory board with the tasks of an audit committee. Notwithstanding the foregoing, the entities wherein audit committees currently operate, must verify whether competencies and professional experience of members of the audit committee, its composition, and internal regulations of the PIE that apply to it, are consistent with the new rules.

When may the functions of the audit committee be delegated to the supervisory board?

Up till now, not all PIEs have been required to create an audit committee. Currently, exemption from such an obligation has been limited to individual cases.

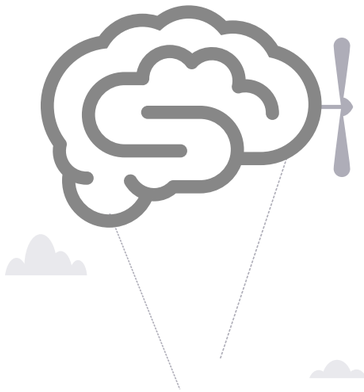
In addition, a PIE had an option to delegate the function of an audit committee to the supervisory board in the event where the board consisted of no more than 5 members.

At present, this criterion has been replaced with new premises, and when assessing the PIE's ability of entrusting the supervisory board with the functions of an audit committee, it is necessary to first examine the criteria enumerated in the Act.

As a rule, PIEs that have not exceeded at the end of a given financial year and at the end of the financial year preceding a given financial year of at least two of the three figures indicated in the Act, may continue to delegate the functions of the audit committee and performance of its duties to the supervisory board or other supervising or controlling body of the PIE. The above-mentioned figures are:

- A sum of balance sheet assets at the end of the financial year amounting to PLN 17m,
- Net revenue from sales of goods and products for the financial year amounting to PLN 34m,
- Net revenue from sales of goods and products for the financial year amounting to PLN 34m, »

Other PIEs which may entrust the audit committee functions to its supervisory board irrespective of size, are cooperative banks, local government units with the PIE status, as well as savings and credit cooperatives that meet the criteria of a large entity.



An additional requirement introduced by the Act is that members of the audit committee should have knowledge and skills of the industry in which the PIE operates. This condition is considered fulfilled if at least one member of the audit committee has knowledge and skills of the industry or individual members have knowledge and skills within the defined scope of the industry.

What requirements do the audit committee members have to meet?

According to the implemented regulations, the audit committee should be composed of at least 3 members, of which at least one should have knowledge and skills in the fields of accounting or auditing. In addition, the majority of audit committee members, including its president, should meet the criterion of independence from the given PIE, as defined in the Act. If the PIE is exempted from the obligation to create an audit committee and entrusts the supervisory board with the function of an audit committee, the requirements set out above must be fulfilled by the members of the supervisory board.

AUDIT COMMITTEE TASKS

The Act also specifies tasks that fall within the competence of the audit committee. These include in particular:

1~ **monitoring** the financial reporting process,

2~ **monitoring the effectiveness of internal control systems,** risk management systems and internal audit,

3~ **monitoring** of auditing activities,

4~ **controlling and monitoring** the independence of the statutory auditor and the audit firm,

5~ **informing the supervisory board, other supervisory or control body of the PIE about the results of the audit and explaining how it contributed to the accuracy of financial reporting in PIE,** and what was the role of the audit committee in the auditing process,

6~ **assessing the independence of the statutory auditor and** giving consent to her/him providing authorized, yet non-audit related services in the PIE,

7~ **developing a policy** for selecting an audit firm,

8~ **developing a policy for providing non-audit authorized services audit** by the audit firm, by entities associated to that audit firm and by a member of an audit firm's network,

9~ **determining the PIE's procedure** for choosing an audit firm,

10~ **presenting a supervisory board** with a recommendation regarding the choice of an audit firm,

11~ **submitting recommendations to ensure the accuracy** of the financial reporting process in the PIE.

Required internal regulations

In accordance with the requirements listed in the Act, the PIE should have an appropriate policy for either an audit firm, an entity affiliated with the audit firm or its network providing additional services, as well as an appropriate policy and procedures for selection of an audit firm.

Notwithstanding the above, PIE may be required to amend its internal regulations defining the rules of appointment, composition and operation of the audit committee.

SANCTIONS FOR NON-COMPLIANCE

For PIE's failure to comply with the requirements introduced by the Act by a set deadline, both the PIE and members of its bodies will face severe penalties. In the case of the PIE, the fine may amount to as much as 10% of net revenues from the sale of goods and products, while the members of its bodies may face financial penalties up to PLN 250 thousand. Members of the PIE bodies may also be subject to administrative penalties imposed by the Polish Financial Supervision Authority, which entail the prohibition of holding office in the PIE bodies for one to three years.

Deadline for implementing changes

The Act entered into force on 21 June 2017. It envisages an obligation to establish an audit committee by PIEs which, according to the provisions of the Act, have a duty to hold one, within 4 months from the date the Act entered into force. Therefore, the deadline for introducing the required changes is 21 October 2017.

Due to the time-consuming procedures required to implement the necessary changes, a PIE should immediately start actions aimed at adapting to the new regulations. ■

PIEs which on the basis of previous regulations were required to have an audit committee, have to, by 21 October 2017, adjust its composition to the requirements set forth in the Act. This obligation also applies to PIEs which, under previous regulations entrusted their supervisory boards with the tasks of the audit committee.

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PRICE-SETTING FORMULAS FOR CLOSING OF CAPITAL TRANSACTIONS

In course of market practice two ways of closing a transaction have been worked out: one based upon the closing accounts and the agreed price formula, which serve as the basis for price calculation, and the other – locked-box, i.e. the price set in advance. Each mechanism has its pros and cons, and their adaptability and effectiveness depend on the characteristics of the particular situation. Therefore, it is good to know which method will be the most advantageous in any given case.

We all make numerous transactions in life. They are generally straightforward, at least when we know the price in advance, and the goods we buy are clearly defined. Of course, it is much more difficult to decide when the item can be seen only in the package, before the purchase, and it furthermore is susceptible to change of value, depending on current internal conditions and market environment.

In the world of capital transactions, the equivalent of pulling out an item from a package before making a purchase is a series of financial, tax, legal, market and operational analyzes, which are referred to as due diligence. Investors know perfectly that one should not 'buy cat in the sack', and before the transaction a 'cat' should be carefully looked at and examined.

The characteristic of capital transactions is the fact that the value of the subject of the transaction can significantly change even within a few days, not to mention the months that usually pass between the moment an investor evaluates it and the time he has taken a full control over the acquired company, i.e. closing the transaction. Such changes may have both a positive and a negative impact on the value of the business and may result from financial operations that the company has recently carried out. For example, significant changes in the value of the company which is the subject of the transaction may arise as a result of a decrease of cash balance, either due to payment of dividends or penalties.

The price formula at the closing of a capital transaction reflects the parties' approach to changes between the valuation date, i.e. the moment of valuation of the company, and the moment it is taken over.

At the time of signing the SPA, the benefits and economic risks associated with the transaction are passed on to the buyer, starting the phase of preparation of closing accounts, on the basis of which the price adjustment will be calculated. Undoubtedly, such a closing accounts, which the seller is normally responsible for, should be subject to verification. Nowadays parties tend to choose an independent advisor to verify the accounts.

Closing accounts
Finalising a transaction based on the closure accounts often pertains to a one-on-one transaction, where there is no other counterparts, in which case the first attempt to set the price formula can already take place at the Letter of Intent phase or the Term Sheet phase. Of course, during a due diligence review, it may turn out that some of the assumptions may have to be changed. It is natural that, as investor's knowledge of the company increases, a pre-determined pricing formula can evolve.
In practice, under this mechanism, the buyer pays the seller the price determined on the basis of the balance sheet forecast as at the date of signing the share purchase agreement ('SPA').

At the time of signing the SPA, the benefits and economic risks associated with the transaction are passed on to the buyer, starting the phase of preparation of closing accounts, on the basis of which the price adjustment will be calculated. Undoubtedly, such a closing accounts, which the seller is normally responsible for, should be subject to verification. Nowadays parties tend to choose an independent advisor to verify the accounts.

The main advantages of finalising a transaction in such a way is a reduction of the risk of change in the value of an enterprise (not reflected in purchase price) occurring between the valuation date and the moment the investor obtains the control. In addition, this method gives the parties a sense that the price resulting from the closing accounts corresponds to the value of the company at the moment of acquisition. The disadvantage of this method is the longer price-setting time (compared to the locked-box method) and generally more aggressive price negotiations that may last until the end of the settlement process, and sometimes even disputes arising due to differences in interpretation of earlier arrangements.

Figure **1**

	CLOSING REPORT	LOCKED-BOX
PHASE OF SETTING AND SIGNING OF AGREEMENT	• FORECAST OF THE PURCHASE PRICES FOR THE CLOSING DATE • SETTING THE PRICE ADJUSTMENT MECHANISM AS AT THE CLOSING DATE • SIGNING THE SPA	DATA *LOCKED-BOX* **BASED ON THE LATEST BALANCE SHEET DATE:** • CALCULATION OF NET DEBT • COMPARISON OF THE NET WORKING CAPITAL AS AT THE BALANCE SHEET DATE WITH THE 'NORMAL' LEVEL OF WORKING CAPITAL ADVANTAGES AND THE ECONOMIC RISK IS TRANSFERRED TO THE BUYER
CLOSING DATE	• PAYMENT OF THE FORECASTED PRICE • BENEFITS AND ECONOMIC RISKS ARE TRANSFERRED TO THE BUYER	THE STAGE OF ESTABLISHING AND SIGNING THE CONTRACT • ACCEPTING THE OFFER • AGREE ON AND SIGNING OF THE SPA
PRICE ADJUSTMENT	• CALCULATION OF THE FINAL PRICE (SURCHARGE OR REFUND OF THE DIFFERENCE BY THE SELLER	CLOSING OF TRANSACTION • PAYMENT OF THE PRICE

VERIFICATION OF THE CLOSING ACCOUNTS

POTENTIAL VALUE LEAKAGE IS SECURED BY THE SPA CONTRACT

Locked-box, i.e. the advantages and disadvantages fixed price
The locked-box method is often used when the company under sale attracts interest of several potential investors. Under this method of transaction settlement, the basis for the valuation of an enterprise is usually a due diligence review performed on the so-called locked-box date (see. Fig. 1).
The key advantages of the locked-box method (for both parties) are price confidence and more simple and faster closing process. It should be noted, however, that a fixed price may also prove to be a disadvantage for the seller if the company's value tend to increase over time – although in such cases the parties may set a mechanism to consider the increase in value of the company between the locked-box date and the SPA signing (for example, an adjustment calculated on a daily basis, reflecting the profit earned by a company in a given period). However, this solution is rarely used. On the other hand, the disadvantages for the buyer include the potential risk of value leakage (for instance due to unforeseen events) and the need for a more detailed and in-depth due diligence process. Such process is the only stage of analysis that serves as the basis for determining the value of the company. In addition, the locked-box method obliges the buyer to specify a definite and final transaction price at the time of submitting an offer, often before the complete information on company is available (in practice at the due diligence stage the seller will not provide all information about the company, especially those that relate to confidential terms of trade). Therefore, when using the locked-box method, buyers should demand more open due diligence and an access to data, stemming from the fact the need to minimize the above-mentioned risk.
The potential risk of a company's value leakage can also be minimized by reducing the time between the locked-box date and the moment the investor takes control of the company as well as by adequate terms and conditions of the deal (mainly resulting from due diligence findings) introduced to the SPA. Nevertheless, it is important to note that under locked-box mechanism, the risk of value leakage is inseparable. This method is often used by Private Equity funds when selling their portfolio because of the simplicity and speed of the transaction, as well as the ease in comparison of attractiveness of the offers made by several bidders.

CHOOSING THE TRANSACTION CLOSING METHOD

It is difficult to clearly state which method of transaction closing is better. The choice of a particular method is, in each case, will depend on, for example, the number of potential investors, the schedule of transactions and the attractiveness of the assets sold. All these factors will translate into the negotiating power of the parties. Due to the characteristics of the two mechanisms, the seller will usually prefer the locked-box mechanism, while the buyer, the price adjustment mechanism. ■

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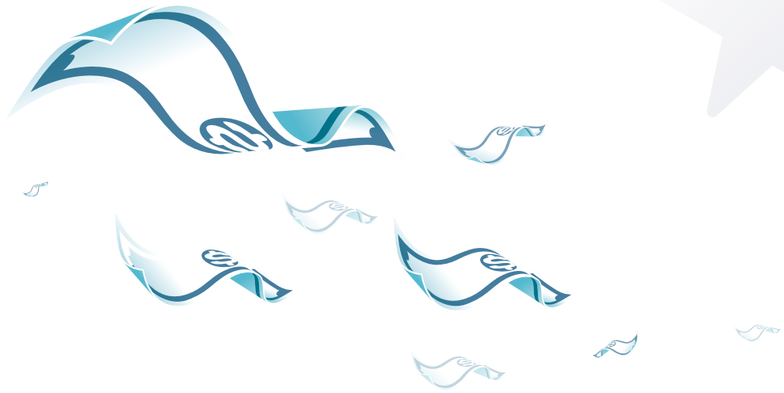
NEW EU SOLUTIONS REGARDING COUNTERMEASURES AGAINST MONEY LAUNDERING AND FINANCING TERRORISM

The new legislation introduces a number of measures to strengthen and tighten Anti-Money Laundering (AML) and counter terrorism financing regulations. Their purpose is also to facilitate institutions obliged to perform their tasks in that areas more effectively, as well as to improve the coordination of inspections carried out by separate units cooperating with the General Inspector of Financial Information.



As of June 25 2017, the so-called Third AML Directive was replaced by Directive 2015/849 of the European Parliament and the European Council on the prevention of the use of the financial system for money laundering or terrorist financing (commonly referred to as the Fourth AML Directive, adopted on 20 May 2015). Due to the multitude of changes introduced by the new EU legislation, the Polish legislator has decided to replace the existing Law on Money Laundering and Terrorist Financing with the new act and not the amendment of the existing law. Below we present the most important changes. Despite the expiry of the deadline for implementation of the new Directive, changes in Polish law have not yet been introduced.

Actual Beneficiary (AB)

To ensure greater transparency and access to information about actual beneficiaries, Member States were required to keep information about them in a central or other public register. That way, every institution obliged to verify the customer / contractor's basic data will be able to check the data contained in all of the registers.
However, in order for such data to be included in the central register, there has to be an obligation in place for the data to be submitted by the business entities. Thus the Fourth Directive introduces the obligation to provide information about AB and to transfer them to the relevant register – it applies also to entrepreneurs who are not subject to AML requirements.
If the AB could not be named by identifying a natural person ultimately exercising control, via ownership or otherwise, over a legal entity, the Fourth Directive allows the obliged institutions to confer such status on the person or persons holding senior management positions. This solution is only possible after exhausting any attempt to obtain such information.
This will mean that the obligated institutions will need to collect evidence and keep documentation that will clearly prove that sufficient action has been taken to determine the AB.

CENTRAL REGISTER OF ACTUAL BENEFICIARIES

The draft of the new Polish Anti-Money Laundering and Terrorist Financing Act provides for the creation of a Central Actual Beneficiaries Register in the form of an ICT system, which will process information on actual beneficiaries of the following entities: public limited partnerships, limited partnerships, limited joint-stock partnerships, limited liability companies, joint stock companies (excluding public companies), foundations and associations.

Risk analysis

The Fourth Directive proposes an anti-money laundering and terrorist financing approach based on risk analysis. On the basis of the current law, this process is carried out at the level of obliged institutions, whereas under the provisions of Directive IV the obligation to carry out risk analysis will also apply to the Member States of the European Union. The European Commission is the first entity required to prepare a proper risk analysis. Successively, Member States and financial institutions will be obliged to do so. For the obligated institution, it will certainly be easier because it will first obtain information about the risks that affect the given country. Under Polish law, a risk assessment at the national level, carried out by the General Inspector of Financial Information will be used to develop appropriate rules for each sector or each area, both in terms of money laundering risk and terrorist financing risk.

Politically Exposed Persons

The Fourth Directive also introduces changes regarding PEP - Politically Exposed Person. It distinguishes three categories of PEPs: foreign, domestic and international. People who hold a prominent public function in a given country and who work in international organizations are also included in the term. After making appropriate changes to the Polish law, it will also be necessary to determine whether the actual beneficiary in question is or is not a person holding a prominent political office.

Financial security measures

The Fourth Directive also tightens the regulations on the possibility of exempting particular categories of entities from the requirement of using the financial security measures. In the Third AML Directive there was an option to unconditionally exempt a specific group of entities (such as public administrations or obligated institutions).
It was considered that obliged institutions took advantage of these provisions too liberally. Therefore, according to the new regulation, exemption from the use of financial security measures can be granted only on the basis of a risk analysis carried out by the obligated institution.

The revised directive also removed the provisions on the positive 'equivalence' of third countries and Member States, with the assumption that geographic exemptions should be less important given the general assumption that the customer vetting system is based on risk analysis.

ADMINISTRATIVE PENALTIES

Basic changes in the use of administrative penalties for non-compliance with anti-money laundering and terrorist financing regulations include:

- **extension of the catalog of sanctions** imposed on obligated institutions
- **extension of the catalog of infringements** subject to sanctions
- **detailing the conditions** affecting sanctions' type and fee
- **introducing the possibility of imposing financial penalty** on the persons performing managerial functions in the obligated institutions
- **defining rules for disseminating information about sanctions** imposed or granting with powers to impose sanctions all bodies authorized to carry out inspections regarding compliance with anti-money laundering and terrorist financing rules

Tightening the rules on third countries

The revised directive also removes the provisions on the positive 'equivalence' of third countries and Member States, with the assumption that geographical exclusions should be less important given the general assumption that the customer vetting system is based on risk analysis. It is now thus impossible to recognize third countries' anti-money laundering systems as 'equivalent' to such systems in the EU. Therefore, obliged institutions will be required to check customers from countries that are now considered 'safe'.

The draft of the new Polish law provides for sanctions in the form of ordering an institution to refrain from undertaking certain activities, in the form of withdrawal of the authorization to carry on the activity of the obliged institution, or even of suspending the performance of duties related to anti-money laundering and terrorist financing, by employees or other persons acting on behalf of and for the obliged institution, responsible for violation of the provisions of the act. Another new feature is the option of publication, in the Public Information Bulletin on the website of the office serving the minister responsible for public finances, information about the obliged institution that has violated the provisions of the law, along with the extent of its violation. As for financial penalties that can be imposed on obliged institutions, they may amount to the equivalent of € 5 million or 10% of the revenue reported in the last audited financial statements for the financial year. ■

An important information for the obliged institutions: according to the new regulations, only serious, recurring and organized infringements will be sanctioned.

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ERA OF EMPLOYEE EXPERIENCE IS COMING – HOW DO POLAND BASED COMPANIES PLAN TO BUILD IT?

Before we enter the era of Digital Labor, where a large number of employees will be replaced by so-called bots, the key issue for many companies nowadays is the question of building the employee experience. How does it look like in Poland?

More than 70% of Executives in Poland identify the employee retention issue as the main priority in human capital management for the coming 24 months. In addition, 90% of them indicate the challenge of uncontrolled staff departure, and the situation is further complicated by the trend in labor cost optimization – still a pending issue in 4 out of 10 companies.

Key Employer Challenges – Poland AD 2017

Board members and Executives of companies operating in Poland indicate the most important aspects in human capital management for the next 24 months.
The key Employer Challenges will be:

- retaining employees,
- attracting candidates,
- employee engagement.

These challenges are priorities for most of the companies, as indicated by about three quarters of managers. The essential factor is in the consistency of this opinion between Board members and HR Managers. Sectors, affected by the employee retention and engagement issue particularly, but facing problems in attracting new candidates, include the following: new technology, heavy industry, retailers, a broad spectrum of service providers and construction, property management. There is a visible trend, that employee experience is increasingly important in smal and medium enterprises.

The transformation of the human capital management function itself is also a serious challenge. The current market environment requires companies to innovate in the human resources function sector, which

on the one hand keeps up to date with management and technological trends, using, among other resources, digital transformation solutions and new technologies in internal communication or data & analytics. On the other hand, management expects from HR function to support business areas in the identification and development of employee potential, investing in design and implementation of applicable intrapreneurship tools.

UNCONTROLLED STAFF DEPARTURES

As many as 90% of the surveyed companies confirmed the problem of the uncontrolled departure of employees. As a result, the focus area has become the development of initiatives and tailored activities aimed at the retention of managers and experts. Another group of companies concentrates its initiatives on reducing the level of uncontrolled departures of its workforces in manufacturing and junior specialists and entry level positions and routine job positions. The high fluctuation of the numbers employees in job positions with relatively short onboarding periods result in higher recruitment and training costs. The cost curve development impacts many companies negatively, becomes precarious, especially for companies located in places with a low-unemployment rate or limited access to candidates with the relevant experience and qualifications. Companies compete for the same employees, while in most of the cases the same budget is allocated for their recruitment, and the budgets are narrow.

Talent managemen

Following the trends, talent management has become increasingly important. According to KPMG in Poland Survey, only about 12% of companies confirm, a formal talent management program is to be adopted. These programs are implemented in large companies, with over 500 employees mostly. The programs, however, are adapted alone in about 40% of Polish companies employing such a large number of people. Banking and financial services, as well as business services (e.g. Business Process Outsourcing Centers) are the sectors in which companies recognize the importance of talent management programs, and use those programs to retain particular group of employees.

A talent management program needs to be designed with flexibility for changes. Companies change the group of identified talents according to market development and internal needs. The Survey shows that talent management programs are less formal in small companies, and usually take the form of ad hoc initiatives. Companies with larger number of employees apply more formal programs, and define the talent vin a different way, those programs are adapted to recent company requirements, i.e., by modifying the criteria and directions.

EMPLOYEE EXPERIENCE PILLARS:

The KPMG approach on theemployee experience is based on the study of employee experience as an internal customer within the organization (equivalent of CX - Customer Experience) and the study of the maturity level of the human capital management function. The Employee Experience Pillars are defined:

1. PEOPLE
2. OPPORTUNITY
3. REWARDS
4. WORK
5. ORGANIZATION

Building employee experience

Human capital management requires a comprehensive approach, based on a multi-faceted analysis of the factors that create the company's unique value. The Employer unique value leads to the development of targeted initiatives and activities aimed at attracting, retaining and developing employees, and should be based on employee experience. Building customer-tailored employee experience within a company, as well as monitoring and verifying employer activities in this area regularly, leads to a decrease in turnover by 69%

The human factor reduces turnover the most

According to KPMG in Poland Survey, the human factor (People) has the most significant impact (3.8 points on a 5-point scale) on the employee experience. Companies recognize the importance of people in building employee experience, and nearly 50% of companies plan to implement measures to improve this area. The greatest importance for employee retention was given to the impact of the quality and competencies of managers. Companies declare investing the most in this area. Employees need to be guided within an organization. Investing in building leadership, especially in line managers and team leaders proves to be not only essential, but above all profitable.

HR Managers declare that they will continuine to invest in designing and developing activities contributing greatly to improving the quality and competencies of managers in the near future. Leadership development programs influence the retention of employees and their team members significantly. Very close and highly rated was matching employee's duties with his/her skills and knowledge (40%) and the employee and his/her team match (39%). Companies are planning to intensify efforts aimed at onboarding programs (35%).

Employee opportunity – the area for implementing new initiatives

The principles of employee evaluation and his/her development are an important pillar of building employee experience. In the coming months, they will both serve as the basis for new initiatives in human resources departments. Companies plan to invest in defining career development paths, leadership and management skills development programs, and other employee training programs.

Base salary as a key factor of employee retention

While weighting the individual pillars of employee experience, remuneration tools came in third place. After analyzing the pillar elements, one can see that the base salary as a single component plays the most important role in employee retention (4.2 points on a 5-point scale). 81% of companies declare to apply remuneration policy based on the industry and local market characteristics. Adapting the remuneration tools further is a priority in this area and is present in the plans in every third of these companies.

Another important subject of this issue is the mechanisms of the variable pay system. 70% of companies report applying variable pay systems. Companies try to keep their payroll budgets at a steady level, thus influencing employee experience perception. This in turn determines whether the employee has an active or passive approach in searching for a new job. In order to properly manage employee experience, companies must implement appropriate organizational effectiveness tools to determine the profitability and productivity of each position, so that they can maintain workforce planning. ■

Employee appraisal is indicated as crucial and the foremost in employee experience for the near future. Nearly 90% of companies specified planned initiatives aimed at the (re)design of employee review and development programs over the next 24 months. Employee appraisal transformation, learning & development initiatives, leadership competencies influencing team management style shall be increasingly imposed by workforce diversity in the labor market. Companies need to adapt to the type of employees and candidate profiles of the labor market.

PENALTY
POINTS

MONITORING YOUR EMPLOYEE IS IT LEGAL?

Both employers and employees periodically get back to questions about the principles of workplace monitoring. Each side has its own perspective on this issue. What monitoring measures are acceptable? How does monitoring look like in the context of the protection of personal data?

Employers look for solutions that allow them to legally control employees, check the quality and effectiveness of their work and ensure the safety of the workplace. It is about organizational and technical solutions, or ways to monitor employees, but also about legal solutions, or what should be done to be able to legally monitor them at all. Employees, on the other hand, are wondering how monitoring affects their right to privacy, confidentiality of correspondence, or to what extent does it reduce their work comfort, limits their freedom or decreases their well-being in the workplace.

EMPLOYEE MONITORING MEASURES

Employers use a variety of employee control measures. Apart from sobriety control, they resort to video surveillance (cameras), monitor employees' activity in the IT network, on the Internet, they monitor computers, phone calls (billings), e-mail, check the GPS installed in company vehicles, and frequently use random personal searches or searches of desks or cabinets carried out by security personnel. The choice of measures will depend on the nature of an organization, the problems that employers face (such as theft), and the interests they want to safeguard, but also on the purpose of controls and, of course, will hinge on certain other conditions.

Monitoring and EU regulations

The topic of monitoring is also emerging in the context of the new EU Personal Data Protection Laws of 2016/679 of the European Parliament and the European Council of 27 April 2016, regarding the protection of individuals in the context of processing personal data, the free circulation of such data and repealing Directive 95/45 / EC (GDPR). On the one hand, GDPR orders personal information to be protected against such incidents as data leaks or theft (which may happen inside an organization through sending them via personal email, a method that is unauthorized, but easy in the technological sense) that, if it occurs internally, can be detected by network monitoring, including monitoring workstations – computers – and employees. On the other hand, GDPR refers to the monitoring of individual persons or the employer-employee relationship quite generally.

Permissibility of monitoring

Monitoring is, in another words, constant observation, control, supervision. Although in the labor law the concept features a conflict of interest (employer versus subordinated employee, security versus privacy), there is no doubt that, in principle, controlling one's employees is acceptable. The question of monitoring has not yet been regulated by the Polish labor law. Practically, the only regulated (though just to a certain extent) form of employee control is sobriety control. However, in both the case law and legislation, monitoring in employer-employee relations is acceptable under certain conditions as outlined below.

How to monitor legally?

From a legal point of view, monitoring in the workplace has to be justified, meaning that the employer should determine the purpose of monitoring employees first.
Acceptable purposes are as follows:

- workplace safety,
- preventing theft,
- protecting the confidentiality and organization's secrets, preventing their disclosure,
- controlling the compliance with the obligation to use e-mail only for work-related purposes,
- protection of personal data within the organization,
- IT system security.

In principle, it is also allowed to control the quality and effectiveness of work, particularly in manufacturing plants.

The purpose should indicate the interests or needs of the employer, and influence the selection of monitoring measures and its scope. Both the means and the scope of monitoring must be proportionate to the purpose or needs of the employer. In addition, the employer must make sure that the target can not be achieved by other, less burdensome means.

Then, once the purpose and the means have been set, the employer must inform the employees about the monitoring before the monitoring begins. The overt monitoring is most common, although case law permits hidden monitoring - on an exceptional basis only, when it serves the purpose that is impossible to achieve using other methods. The information is best conveyed to employees in the form of a written statement that an employee is required to sign (a matter of proof), and the relevant provisions should be included in the rules of employment or the rules for the use of workplace tools.

It is assumed, for example, that e-mail monitoring can not entail constant surveillance of an employee's workplace mailbox. Obviously, when it comes to video surveillance, it is necessary to designate a camera zone, excluding areas such as locker rooms, toilets, canteens, and smoking rooms where workers should enjoy their privacy. Generally, the control of employees in any form can not unduly interfere with employees' privacy.

Monitoring and personal data protection

As a result of the monitoring, the employer may collect a scope of information about his/her employees and there is no doubt that much of that data may be personal. Therefore, monitoring should also be considered from the point of view of personal data protection. As a matter of fact, an employer must prove the existence of a legal basis – in principle the only possible one in this case, that is the existence of a justified purpose.

Of course, it is necessary to meet the information obligation (the purpose and scope of the data being processed within the control) and other obligations, in particular the one to providing data security. As for the issue of data set registration (until the Polish Act on Personal Data Protection is in force): the legislation assumes that information obtained through monitoring (for instance, camera footage) will fall within one of the exceptions from the registration obligation, ie. in the case of processing data related to recruitment. Employee-sensitive data (such as those disclosing political views) should not be collected and if they were recorded via monitoring, they should be removed.

Providing employees with the ability to exercise their rights, such as the right to be forgotten or the right to correct data, seems to be a much more difficult. The issue of correcting data in case of video surveillance is important.

The subject of employee monitoring is also worth pursuing in the context of GDPR mentioned above, particularly as monitoring is one of the foundations for impact assessments of data protection. ■

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LACK OF TRANSFER PRICING DOCUMENTATION MAY RESULT IN SANCTIONS

PENALTY
POINTS

Due to the new transfer pricing regulations having entered into force, the scope of duties of taxpayers involved in related party transactions has significantly expanded. Failure to do so may result in serious penalties imposed both on the taxpayer and the so-called liable persons.

Taxpayers making deals with related parties are obliged, among other things, to prepare tax documentation and to make a statement on its preparation. The risk of liability for failure to meet these obligations is established at two levels: at the company level as a taxpayer and at the natural person level, responsible for fulfilling company's obligations.

Income adjustment
According to Art. 11 of the CIT Act transactions between affiliated entities should be carried out under conditions to be determined by independent entities in the same circumstances (the arm's length rule). If the tax authorities conclude that the terms of transactions between affiliated parties are not in line with the arm's length principle, they will be eligible to adjust income up to market-level.

PENALTY TAX RATE

If the income becomes assessed and the taxpayer fails to submit tax documentation to the tax authority, the difference between the taxable income declared by the taxpayer and the amount calculated by the tax authority will be taxed on the basis of Art. 19 sec. 4 of the CIT Act at the rate of 50% instead of the basic rate of 19%.

Personal responsibility
In keeping with the announcements of the Ministry of Finance, we are witnessing intensified interest of tax authorities in the verification of tax settlements. Not only a large increase in the number of started controls, but also a significant increase in their effectiveness is clearly visible. Irregularities in the settlements revealed during inspections often lead to commencement of proceedings against the so-called liable persons.

1. PENAL FISCAL LIABILITY

The risk of penal fiscal liability rests with persons obliged to act on behalf of the taxpayer, that is: members of the board of directors, chief financial officer or chief accountant.

Legal basis of fiscal penal liability:
Penal fiscal qualification of failing to meet transfer pricing obligations, is not, however, obvious. The legal basis for liability may be:

A) REGULATIONS RELATING TO TAX INFORMATION

Bearing in mind that the tax documentation is based on Art. 9a of the CIT Act, considering it tax information seems to be the most appropriate approach. Failure to submit the required tax information and the submission of untrue information to the competent authority is punishable by a fine pursuant to Art. 80 § 1 or 3 of the Penal Fiscal Code (PFC). Maximum fine imposed pursuant to Art. 80 § 3 of the PFC in relation to Art. 23 § 3 of the PFC amounts to PLN 6.4 million.

B) REGULATIONS CONCERNING BOOKKEEPING

If the tax documentation is treated as official books, failing to present it to the auditors within seven days of the date of the summons may be deemed as obstruction of a tax audit. The basis of liability will in this case be Art. 83 § 1 of the PFC, and fine pursuant to Art. 83 § 1 of the PFC in relation to Art. 23 § 3 of the PFC can amount to as much as PLN 19.2 million.

C) REGULATIONS RELATING TO THE FILING OF DECLARATIONS

On the other hand, the legal basis for the penal fiscal liability for submitting a false statement regarding the preparation of complete tax documentation may be constituted by Art. 56 § 1 of the PFC. Maximum amount of fine imposed pursuant to Art. 56 § 1 of the PFC in relation to art. 23 § 3 of the PFC amounts to PLN 19.2 million. Moreover, the above-mentioned infringement in its basic type can also be subject to the penalty of imprisonment – both as a self-standing punishment and as a joint penalty of a fine and imprisonment. According to art. 27 § 1 of the PFC, imprisonment may last not shorter than 5 days and not longer than 5 years.

2. CRIMINAL LIABILITY

Art. 296 § 1 of the Criminal Code (CC) imposes the imprisonment penalty on a person, among others, who was obliged to deal with property or economic activity of a given entity and through abuse of powers granted to him or through failing to comply with his duty causes significant property damages (i.e. property damage exceeding PLN 200 thousand).

Applying a 50% penalty to the company and consequently causing the necessity to pay a higher tax may be considered a significant property damage to the company (or even substantial property damage, i.e. over PLN 1 million). Causing economic damage is punishable by imprisonment of up to 10 years (in case of substantial property damage).

3. TAX AND CIVIL LIABILITY

In the limited liability company the risk of personal liability for the company's tax obligation is borne by the members of the board pursuant to Art. 299 § 1 of the Commercial Companies Code (CCC) according to which if the execution against the company proves ineffective, board members are jointly and severally liable for its obligations.

The basis of liability of board members towards the company itself for the damages in the form of the requirement to pay a higher tax is Art. 293 § 1 of the CCC and Art. 483 § 1 of the CCC. The above provisions do not violate the rights of shareholders and third parties to seek redress under general principles.

This is a conditional liability that in the event of failure to comply with the obligations arising from the transfer pricing regulations will come into force when an additional income taxable at a rate of 50% is adjusted to the company and when execution of tax obligations against the company itself proves to be ineffective. In such case the board members will be personally obliged to pay the tax on behalf of the company.

Guilt as a condition of liability

In criminal and fiscal proceedings there are different rules than for example in tax proceedings - violation of the tax law does not have to be unequivocal with committing a crime, a fiscal crime or fiscal offense. Bringing a perpetrator to justice on the grounds of criminal liability or penal fiscal liability has been conditioned on assessing perpetrator's guilt at the time of committing the offense. One of the procedural guarantees of the above notion is the principle of the presumption of innocence. As a consequence, in case of criminal or penal fiscal liability, the official body must prove the perpetrator's guilt. The accused is not obliged to prove the absence of guilt.

The distribution of the burden of proof, however, is different in the case of liability of a member of the board of directors of a limited liability company for its obligations under Art. 299 § 1 of the CCC. This provision imposes a presumption of guilt of a board of directors member who may be released from liability if he provides one of the conditions set forth in Art. 299 § 2 of the CCC.

Non-market nature of pricing vs. liability

It seems that these two conditions must also be fulfilled in case of, for example, prosecuting a member of the board of directors for infringements of obligations regarding transfer pricing under Art. 296 of the CC or Art. 299 § 1 of the CCC. On the other hand, the conditions of penal fiscal liability are different.

The condition of penal fiscal liability is culpable failure to perform obligations or improper carrying out of obligations imposed on the taxpayer. This liability does not depend on whether the taxpayers' prices are market prices. Consequently, fiscal penalties can be imposed even if intra-group transactions are in line with the arm's length principle. ■

Given the increased scope of responsibilities of taxpayers making transactions with affiliated entities, the increasing number of tax audits, and the possible legal consequences of infringements, it is recommended that taxpayers introduce appropriate procedures to deal with transactions concluded between affiliated entities. Such procedures should make it easier for taxpayers to meet their transfer pricing obligations on time.

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