

## TAX EXPLANATIONS CONTRA LEGEM

A public consultation on the Polish Ministry of Finance's draft Tax Explanations of 25 September 2023 on withholding tax (the "Draft") commenced recently.

The Draft includes, inter alia, clarifications of the concept of the "beneficial owner" of receivables liable to withholding tax (the "WHT"), since only income received by an entity that is the "beneficial owner" of dividends, interest or royalties may be subject to tax exemption or more lenient taxation in Poland. It was pointed out in the Draft that the "beneficial owner of the receivable" is an entity that receives the receivable for its own benefit and is not merely an administrator of that income, i.e. the recipient receiving the receivable on its own behalf, but in the interest of and for the benefit of another entity. In the Draft, it has been pointed out that certain external or economic circumstances may indicate that the recipient is acting as an 'income administrator', which will exclude the application of the exemption from WHT.

### Taxpayer-dependent reasons

The Draft lists many examples of circumstances that preclude the recipient of a receivable from being considered the 'beneficial owner'. Many of these circumstances are a manifestation of the way of management of the amounts received and shaping its business by the recipient. Among others, the Draft identifies such circumstances:

- the exclusive object of the entity is to receive receivables and passing them on,
- receivables are transferred to another entity at short intervals,
- payments of receivables occur at regular intervals,
- the entity does not reinvest funds received<sup>1</sup>.

Undoubtedly, the recipient of the receivables has an influence on the formation of the circumstances indicated above. It will depend on the receiver of the amounts whether he is engaged in a wider earning activity or merely "receiving receivables and passing them on" or whether the entity "does not reinvest the funds". I leave aside at this point my own assessment as to whether these examples are accurate in light of the current legislation and focus solely on the possibility that these circumstances may arise as a result of an act or omission of the receivable recipient.

### Macroeconomic considerations and considerations beyond the control of the taxpayer

Several examples presented in the Draft refer to circumstances that will not depend on the decisions and activities of the receivable recipient to arise. I refer to the following circumstances:

- "the entity is located in a jurisdiction with an extensive network of double tax treaties or applying preferential tax treatment of passive income from foreign sources,"<sup>2</sup>
- "the entity has its residence in a country ranking high on the list of direct foreign investment in the territory of Poland, mainly due to cross-border provision of financial services, rather than commercial or manufacturing activities, and at the same time, there is no commensurability between the size of that country's GDP and the scale of investments carried out from its territory."<sup>3</sup>

This kind of interpretation, if adopted in the explanations in question, would be a contra legem interpretation, violating a number of tax provisions, including, first and foremost, the principle of tax justice and, in particular, Article 2 of the Constitution of the Republic of Poland, as well as the constitutional principle of primacy of literal interpretation and another principle expressed in Article 217 of the Constitution, according to which taxes have to be levied only by statutes.

<sup>1</sup> See. Project, page 4

<sup>2</sup> Project, page 5

<sup>3</sup> Project, page 5

First, it is true the legislator is free to determine the conditions under which the tax exemption may apply. However, the conclusion that the income is taxable and the withholding tax exemption is not applicable on the basis of the circumstances indicated in the Draft would result from criteria that were not expressed in tax laws (statutes). This is because there is no standard in the current legislation that would make the liability for withholding tax dependent on the circumstances indicated in the Draft, relating to the macroeconomic dependencies and sources of GDP of the foreign taxpayer's country of residence or to a number of double taxation treaties concluded by the taxpayer's country of residence. Secondly, within the framework of the freedom of statutory design of tax exemptions, the legislator should make the application of reliefs subject to "conditions possible to be met by the taxpayer" (e.g. judgment of the Supreme Administrative Court of 13 June 2018 II FSK 1630/16, LEX 2534925). Meanwhile, on the basis of the interpretation under discussion, the taxpayer will not have any influence on the structure of GDP in its country, nor on the existing extent of direct investment in the payer's country in a given period, on which the taxation of his income would depend under the Draft. Nor does it affect the number of contracts concluded by the country of residence. As a result, the interpretation proposed in this respect in the Draft, referring to such non-statutory circumstances and conditions for the application of the WHT exemption independent of the taxpayer's activities, which the taxpayer cannot fulfil, grossly violates the constitutional principles.

### **Do the examples of macroeconomic reasons indicated in the Draft confirm the to-date practice of legal and tax advisors, tax authorities or administrative courts?**

One may ask this question in order to determine whether the Draft is intended to sanction the previous (erroneous in my view) practice of the advisory community, tax authorities and courts. Nevertheless, I am not aware of anyone previously expressing similar views, according to which the application of the withholding tax exemption would be determined by similar macroeconomic considerations, resulting from the financial and economic situation of the country, which by their nature are subject to change, also during the tax year, and are beyond the taxpayer's ability to influence them. So far, I have not encountered similar views from the tax authorities either, despite the fact that I have been dealing with tax matters for several decades. Therefore, it is my opinion that the exemplary reasons for refusal to apply the tax exemption proposed in the Draft do not result from the previous practice or the applicable regulations, despite the fact that the tax explanations are supposed to perform the function of interpreting the regulations and not the normative function. Therefore, the relevant parts of the Draft of the Tax Explanations should be removed from the Draft as soon as possible or substantially amended.



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