

Tax briefing Poland



POLISH TAXATION OF PROPERTY INVESTMENT BY FOREIGNERS

The purpose of this document is to outline the general taxation issues which can have an effect on the rate of return from investment in property in Poland. It deals both with short term investment for resale (or primary development) and with long term investment. It is recognised that in many cases investors will wish to develop a property, install tenants and then sell to an institutional investor. We are also aware of the significant interest in the purchase by private investors of commercial properties from the investment portfolios of developers.

Historically investment has been routed via a Dutch special purpose vehicle (SPV) to take advantage of the possibility of realising a gain which was not taxable in Poland under the provisions of the Polish – Dutch avoidance of double taxation treaty (DTT) which exempted from taxation in Poland the sale of shares in a Polish company whose major asset is property. However the ability to use this tax planning scheme has been significantly restricted and potential clients are strongly advised to consult with their tax consultants in their home jurisdiction on the implications on their own tax

position of owning property in Poland via an intermediate

Entity. Increasingly investment via a branch of an EU resident corporation is becoming popular as well as property holding via a limited partnership (spółka komandytowa).

This document only sets out the tax consequences in Poland. The implications on taxation in the home jurisdiction of the investor will depend on the tax regime in their home country as well as on their own particular circumstances. We will be pleased to advise clients in

conjunction with their own home jurisdiction tax advisers. As with all tax planning solutions which are optimal today may, with the passage of time and changes in tax legislation and tax rates, prove to be more expensive long term. We draw attention to the fact that tax rates in Poland could change in the future.

The accession of Poland to the European Union (EU) has significantly improved the prospects for investment in Polish property and the market (and in particular the secondary market) has seen significant activity particularly by foreign pension funds.

Possible forms of investment

Foreign entities and foreign nationals can invest in property using the following legal entities:

- Limited liability company (Spółka z ograniczoną odpowiedzialnością – Sp.z o.o.)
- Joint stock company (Spółka Akcyjna – S.A.)
- Limited partnership (Spółka Komandytowa)
- Branch

In practise a branch was not recommended in the past as the tax offices can seek to tax in Poland profits properly attributable to economic activity outside of Poland and there are also problems with the documentation of attributable costs. This can lead to lengthy tax investigations which are difficult to defend and take up considerable management time. However with Poland's accession to the European Union and in particular access to the European justice system the excesses of the Polish tax authorities have been tempered.

In addition foreign nationals can invest directly as individuals or under a registered economic activity (działalność gospodarcza).

Purchase of land

Permission is required in most cases for foreign entities and foreign individuals to purchase land in Poland and also for foreign entities and individuals to hold more than 50% of the shares in a Polish company which as an asset has land. Permission is obtained from the Ministry of the Interior and Administration. The process can take several months to complete and may require the agreement of other Ministries.

Permission is given in respect of a specified property. Permission is not required to purchase apartments nor land up to 4,000 square metres for the purposes of building a manufacturing plant.

From 1st May 2004 permission is not required in the case of purchases by citizens of the EU, Norway, Iceland and Lichtenstein and by legal entities resident in the EU, Norway, Iceland and Lichtenstein. Restrictions still apply to EU, Norway, Iceland and Lichtenstein citizens in respect of the purchasing second property in Poland used for own housing purposes. The purchase of agricultural and forestry land by EU, Norway, Iceland, Swiss and Lichtenstein entities and nationals still requires permission.

At present there are no instructions for notaries to check the share ownership structure of an EU, Norway, Iceland and Lichtenstein resident entity which in practise will mean that a US citizen, for instance, can acquire land without permission via an EU, Norway, Iceland and Lichtenstein resident entity.

Legal form of purchase

Purchase requires in all cases the signing of a notarial deed with the vendor on which stamp duty of 2% is payable plus a further amount of close to 2% in notarial fees (the overall amount is capped and negotiation of the notarial fee is possible particularly with high value transactions. The registration of a mortgage charge amounts to 200PLN. The charges are normally (by custom) borne by the purchaser but the liability is joint and several with the vendor.

Corporate and personal economic activity consisting of ownership and development of land

Businesses can elect as to the accounting consequences of an investment. The choice is between holding the land and any buildings on that land as an investment destined to produce rental income (the asset is disclosed as a fixed asset) and holding the asset as stock in trade destined for resale (the asset is disclosed as trading stock).

In the past the choice of accounting determined whether

VAT on construction costs could be recovered rather than carried forward for offset against future output tax. This was only possible in the case of investment activity using the rules for the recovery of VAT incurred on the acquisition of fixed assets.

Under changes in the VAT legislation effective from 1st May 2004 excess input VAT can be reclaimed in all cases (except in the case of partial or total VAT exemption of sales) whilst previously the reclaim was limited to VAT related to the acquisition of fixed assets and in the case of sales at lower rates of VAT. However the tax office has 180 days to refund VAT under general principles and 25 or 60 days in relation to the old principles (which continue to apply). In many cases therefore it will still be beneficial from a cash flow perspective to treat the property as an investment (and will be compulsory if the investment is in domestic property).

Clients are advised that proper books of account compliant with Polish law have to be maintained on a current basis, in the Polish language and kept in Poland. Because of the monthly reporting of all taxes (with the exception of small businesses which can elect for

quarterly returns) the cost of bookkeeping services is higher than in other jurisdictions.

Construction of domestic property for rental

The rental of domestic property is VAT exempt which means that input VAT cannot be reclaimed except in the case of VAT incurred for construction of the flats where there is an intention (proved by fact) to realise at least some VATable revenue. Therefore to reclaim input VAT in the construction or acquisition phase at least one of the apartments must be designated for sale rather than rental as domestic premises (the sale is VATable at 8%). The construction of domestic property destined for rental by the investor should therefore be treated as an investment property and VAT on construction costs reclaimed under the old principles and then clawed back overtime.

Taxation of rental income in the case of a corporation

The current rate of corporation tax is 19%. The tax basis is calculated after deducting tax allowable costs which include

depreciation of buildings and infrastructure but not land and can include interest on loans taken to acquire the property. Please note however that for tax purposes interest accrued in the period of construction increases the value of the property. Interest is only tax allowable however when actually paid.

Depreciation can be claimed on the value of buildings but not land at the rate of 1.5% (residential), 2.5% (commercial property) and 4.5% in the case of infrastructure) per annum. Higher depreciation rates can be claimed in respect of any plant and equipment (e.g. air conditioning, lifts etc.) if separately identified. Buildings purchased when more than five years old can be depreciated over a period of 10 years. However, in the case of the commercial property for which the depreciation rate is 2,5% - 40 years less the number of years which passed from the first day of using them (this period cannot be shorter than 10 years).

Rental income on property is always taxable in Poland

Taxation of capital gains on sale of property by a corporation

The profit on disposal (net sale proceeds less tax written down value of property and less any costs of disposal such as agent's fees) are cumulated with other sources of income and taxed at the general rate of 19%. There are no indexation allowances in respect of the effects of inflation.

Payment of corporation tax

Corporation tax is payable in Poland monthly on account and is based on tax at 19% on cumulative taxable profits less the amount of tax paid on account in previous months of the tax year. The tax year normally ends on 31st December unless the entity has elected for a different financial accounting period. This means that full accounting records have to be maintained throughout the year.

Distribution of profits by a corporation

Profits can be distributed by way of dividend. The dividend is limited to the amount of undistributed profits brought forward plus realised profit in the current year less any uncovered accumulated losses brought forward. The dividend is paid following a resolution of

the Annual Meeting of Shareholders.

It is also now possible to pay a dividend during a financial year but only up to one half of current year's profits plus undistributed reserves less any uncovered accumulated losses.

Withholding tax of 19% of the gross distribution is payable unless a relevant avoidance of double taxation treaty provides otherwise.

From 1st May 2004 the payment of a dividend to an EU entity (other than Polish registered) is free of withholding tax subject to the corporate shareholder having held at least 15% of the basic share capital for more than 24 months.

To take advantage of exemption or reduced rates of withholding tax the paying entity must hold a valid certificate of tax residence of the recipient.

Directors remuneration

Directors of a Polish entity who are not tax resident in Poland are generally subject to flat rate tax of 20% on management board and supervisory board member remuneration so long as this does not arise under a contract of employ-

ment. The payments are a tax allowable expense of the company. However, if present in Poland for more than 183 days, they will be liable to higher rate tax at the year end.

Interest on loans from connected entities and individuals

Under current Polish Corporation Tax rules interest on the part of a shareholder loan which exceeds three times basic share capital is disallowed as a cost for tax purposes. The relevant shareholding covers any connected party.

This problem in financing operations can at present be avoided by:

- Ensuring that the loan is not granted by a shareholder or connected entity
- The parent entity or individual guaranteeing its Polish subsidiaries banking facility
- Back to back deposits and bank loans
- The rules will most probably change in 2015

Sale of a foreign entity whose major asset is land in Poland

This is a transaction which is taxable in Poland. However, there are a few Avoidance of Double Taxation Treaties, according to which the gain on sale of shares is to be taxed in the country where the shareholder is tax resident.

Taxation of rental income on property owned by an individual

The general principle is that the rental income net of allowable costs is taxable at progressive rates of income tax (currently 18% and 32%). The tax has to be declared and paid by the individual on a monthly and quarterly basis (there is no requirement at present for the tenant to withhold tax).

An individual may however elect for the gross rental income to be taxed at a flat rate of 20% (with the first 4,000 Euro of rental income being taxed at 8.5%). The tax is assessed on gross rental income (net of any VAT) with no deduction of any costs. An election has to be made in respect of each rental contract at the

latest on the day of receipt of the first payment of rent. The election can be made in respect of individual properties so for instance properties where the tax allowable costs are high can be left to charge under general principles.

An individual who rents out property as part of a registered economic activity may elect for the profits of that economic activity to be taxed at a flat rate of 19% rather than the general principles of progressive rates of tax. A relevant election has to be made on commencement of activity and prior to any income being generated.

Allowable costs include repairs (but not improvements which will increase the depreciable value of the building) and in certain cases interest on loans.

Depreciation allowances are calculated on the same basis as for corporation tax purposes (see above).

Rental income is in all cases taxable in Poland.

Sale of property by an individual

If property is held as part of economic activity the profit on sale is taxable (i.e. after deduction of acquisition cost) either on general principles or at 19% if the relevant election was made when registering the activity.

The tax is payable in the month following the month of sale.

The gains on sale of property are always taxable in Poland.

Registration of economic activity

This is a formal process without which a foreign national may not conduct economic activity in Poland.

Various documents will need to be produced authenticated by the relevant Polish Consulate and translated into Polish.

From 1st May 2004 citizens of the new EU members and UK, Ireland, Sweden, Finland, Greece, Spain, Portugal, Iceland and Italy may take up paid employment in Poland but still require to register an economic activity if any activity other than employment is to be performed in Poland. A residence card, in

this case of non EU nationals, will be required unless the individual leaves Poland each weekend or the stay in Poland in any year is less than 3 months.

Minimum social security contributions may be payable by the individual depending on circumstances.

Transfer of funds abroad by an individual

These can be freely transferred if obtained from documented sources. The transferring bank is required to ensure that any relevant Polish tax has been paid on income.

Funds brought into Poland via an authorised bank can be freely remitted back.

Taxation of limited partnerships

The profits of a limited partnership are taxed according to the tax principles applicable to each of the partners on their share of profits. Thus a corporate partner will be taxed according to corporation tax principles and an individual partner according to personal income tax principles and rates. An individual partner may register economic activity and elect for

the flat rate 19% entrepreneurs tax. As of 1st January 2014 joint Stock Partnerships became taxable in their own right as corporations.

Taxation of non tax domiciled individuals

The first principle of Polish personal taxation is establishing whether an individual has a permanent residence (fiscal domicile) in Poland or not. This is a test of fact and ultimately of long term intention. The nationality of an individual is not of itself relevant (although it is one of the "tie breaker" tests under most double taxation treaties). In the case of individuals domiciled in a country with which Poland has signed an avoidance of double taxation treaty the treaty itself will normally define whether an individual has a permanent residence in Poland or abroad. In the case of individuals domiciled in non treaty countries the test is more difficult as Polish law does not clearly define permanent residence.

Polish personal taxation imposes an unlimited world-wide tax liability on all individuals whose permanent residence is in Poland and on those who are resident in Poland for more than 183 days in any calendar year. All others are subject to

limited tax liability which taxes income arising in Poland and also income from employment where the duties of employment are performed in Poland. Non Polish income is not then subject to tax. The main advantage is that in the case of limited tax liability remuneration as a management board or supervisory board member of a Polish entity is taxed in Poland at a flat rate of 20%. Relevant avoidance of double taxation treaties may also modify the tax treatment of other sources of Polish income.

VAT

From 1st May 2004 the sale of land by a VAT registered entity or individual is subject to VAT at 23%. Other transactions in land are outside the scope of VAT.

The sale of commercial buildings is subject to VAT of 23% Domestic property on the primary market (i.e. sold by a developer or builder) is taxed with effect from 1st May 2004 at 8%.

The sale of property by a VAT registered entity or individual which has been used for more than 5 full calendar years is VAT exempt, if the supplier has not reclaimed VAT on acquisition or construction. The

sale of domestic property which has been occupied for any period of time as a dwelling is free of VAT.

Rental of domestic property by a VAT registered entity or individual is VAT exempt. Rental of other property by a VAT registered entity or individual is subject to VAT of 23%.

Conclusions

The investment in a portfolio of domestic properties destined for rental will, in practise, require the formation of a special purpose Polish legal entity or limited partnership for each development.

The investment in commercial property and the activity of a developer of domestic property for sale can be carried out personally preferably through a registered economic activity.

Clients are advised that the tax law and tax rates may change and in particular that the 19% elective rate of taxation on personal economic activity could be withdrawn in subsequent tax years.

PKGT Audyt

We have extensive experience of providing advisory services to investors in property including tax planning, partner search, sourcing of financing

and tax compliance and outsourced accounting and administrative support functions. We work closely with the leading property agents, property management companies and law firms and notaries providing clients with a complete support service.

The above details are general and for information purposes only. Clients wishing to place reliance on the above information should seek individual advice specific to their own circumstances. They should also obtain advice in their home jurisdiction on the impact of Polish taxation on their global tax position. PKGT Audyt does not accept any liability for actions taken in reliance upon the above information.