

June 2019

## Withholding tax (WHT) – draft of the Explanatory Notes from the Minister of Finance

**On 1 January 2019, restrictive provisions on withholding tax collection came into force. The application of certain provisions was partly postponed until 30 June 2019.**

**On 19 June 2019, the Ministry of Finance (MF) published the long-announced draft of the Explanatory Notes to these provisions.**

### What it is all about

The new regulations in force from January 2019 stipulate that the basic model is for the tax remitter to collect WHT using domestic rates, without deductions under directives or double taxation treaties (DTT), and to apply for a refund afterwards. By way of exception, the tax remitter may return to the relief at source mechanism if he lodges a statement or requests a clearance opinion. This relates to payments to one taxpayer exceeding PLN 2 million in aggregate. Regardless of the amount of the payment, the tax remitter is obliged to ensure due care. At the same time, the definition of the beneficial owner has been specified in more detail.

Currently the MF is trying to explain the regulations which were rushed through the parliament.

### Role of Explanatory Notes and the drafts phase

The Explanatory Notes are a form of explaining by MF how taxpayers and tax remitters should proceed when applying the new regulations in practice.

Acting in line with the Explanatory Notes may give protection such as acting in line with the tax rulings. However, due to the rather general nature of the Explanatory Notes and the multitude of factual statuses, in practice, they play an explanatory rather than a protective role.

For the time being, the MF has published a draft of the Explanatory Notes, inviting to comment by 30 June. This is a very short deadline, but KPMG intends to participate in those public consultations.

In the Explanatory Notes, the MF claims that the document does not modify the principles of previous rules for determining the withholding tax (exemptions, rates, etc.) and orders the tax authorities to apply the regulations taking into account rationality and real possibilities available for the tax remitter to collect and present evidence and to analyse the taxpayer's situation.

Despite almost 40 pages delivered by the MF, the document rather describes the extensive justification for the changes introduced, it still however provides some important guidelines.

### Tax collection and refund

The Explanatory Notes confirm that taxpayers are required to calculate the potential excess of the PLN 2 million threshold regardless of the fact that some provisions were postponed until the end of June 2019 – i.e. all payments should be summed up from the beginning of January 2019,

regardless of the tax year the taxpayer has, and if the payment made after 1 July 2019 exceeds the threshold of PLN 2 million together with the payments made earlier, the tax should be collected according to the new rules.

It is essential also to receive a confirmation on how to apply the new rules for payments to transparent companies – the MF expects that the threshold of PLN 2 million will be applied to payments to individual partners of such an entity.

However, if taxpayers (tax remitters) wish to obtain a refund of the tax paid, they will have to initiate two separate procedures – for receivables below PLN 2 million and for receivables above this threshold (even if it was a single payment).

### Tools for "relief at source"

The MF confirms that the statement for the reduction (exemption) of the WHT must be made at the latest on the day of the payment. It will therefore no longer be possible to benefit from the Directives or the DTTs and to collect tax residence certificates after the end of the relevant year. The MF also explains the method of signing such a statement in the case of a multi-person management board – electronic signature of one member of the management board is required and enclosing a copy of the document with statements of the others. However, there still is no explanation how to sign the documents concerning companies'

branches or entities with a management board consisting also of corporate entities.

As regards the opinion on the application of the exemption (which allows the use of a WHT exemption up to 36 months), it follows from the Explanatory Notes that the MF will not oppose submission of statements under Article 26(7a) after requesting the opinion and before obtaining it. It has been confirmed that the clearance opinion will not apply to the benefits from the DTT but only to the benefits (exemptions) from the EU Directives.

It will be possible to apply for an opinion (similarly, to apply for a tax refund) not only by the taxpayer, but also by the tax remitter, if the tax remitter has incurred the cost of the tax from his own resources. The MF will not expect the contract to include a gross-up clause if the need to gross up is necessary for the business situation. However, in another part of the Explanatory Notes, the MF confirms the right to deduct the WHT cost for CIT only in respect of the existing gross-up clause and not in respect of the "business" gross-up. Therefore you should examine the content of the existing gross-up clauses in the contracts concluded.

#### **The beneficial owner and genuine business activity**

It has been confirmed that the MF would expect that the beneficial owner test would also be met for payments which do not contain such a criterion in DTTs.

Much of the text has been dedicated to intermediaries in the context of the beneficial owner test, where it is again apparent that the unfortunate translation of a "conduit company" as an 'intermediary' can lead to negative consequences for many business areas (e.g. brokers), which, however, carry out real activities, conclude transactions on their behalf and are responsible for the payment they receive, and only the specificities of their business require the costs of the final service provider to be covered from the funds received.

MF emphasizes that the confirmation of the genuine business activity impacts the beneficial owner test.

Useful information in this area may be found in the Explanatory Notes for entities operating shared services centers or collective rights management organizations. In both cases there is a greater understanding of business reality by the MF and of the necessity to use unconventional solutions in the field of taxes. The need to take into account the specific nature of collective copyright management activities was raised by KPMG in the course of previous public consultations. Therefore, it is a significant progress in the MF approach to business diversity.

On the other hand, doubts about the beneficiary's test may be deepened in the case of entities incurring re-invoiced expenses or holding companies.

#### **Due Care**

The MF acknowledges that there are differences in gathering information and documentation from related parties and from non-related parties, as the latter may not disclose their business secrets. As regards related parties, the MF expects to collect detailed information such as financial statements, organisational structure or information on employees and their qualifications – as it is easier to structure a transaction within a large group than in the case of relations with third parties.

Ensuring due care will be necessary regardless of whether the payments exceed the threshold of PLN 2 million. However, through the Explanatory Notes, the MF wants to introduce safe harbours for payments of smaller amounts – which we suggested during the public consultations. For example, for payments not exceeding several tens of thousands of PLN, due care would be maintained by possessing a certificate of tax residency. If the payments do not exceed several hundred thousand, the MF claims that it should be sufficient to obtain a certificate and a statement on satisfying the conditions for tax exemption.

It is however worth to note that the MF expects higher standards of the due care, if the statement according to the Article 26(7a) is submitted. The above list of standards should rather be understood as the necessary minimum.

Our assumptions are also being confirmed that the MF in the framework of due care will expect not only collecting evidences, but also conscious "soft" verification – the establishing of the existence of genuine headquarters at the place of address, the existence of the management board members and their telephones, preparation of the questionnaires on the nature of transactions, comparing the data contained in documents and correspondence with the agreements and invoices.

Certain difficulties may arise for entities making payments to jurisdictions which do not impose WHT on outgoing payments (e.g. Cyprus, Malta or in some cases the Netherlands).

#### **We invite you to contact us**

The Explanatory Notes also contain a number of other elements that may be relevant depending on the type of the business you're running.

We are currently analyzing the draft Explanatory Notes in connection with the public consultations process.

#### **We invite you to contact your local KPMG contact.**

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