September 2019

The Act amending certain regulations in order to limit payment backlogs signed by the President

On 6 August 2019 the President signed the Act amending certain regulations in order to limit payment backlogs (hereinafter: "the Act").

According to the explanatory memorandum to the Act, the main objective of the amendments is to improve the legal environment in which the parties to commercial transactions operate in order to limit payment backlogs.

The Act modifies a number of legal acts, including the Payment Terms in Commercial Transactions Act, the Corporate Income Tax Act (hereinafter: "**CIT Act**") or the Personal Income Tax Act.

The new regulations introduce to the income tax acts regulations concerning the so-called "bad debts" - similar to the solutions already functioning in the Act on Value Added Tax ("**VAT**").

Implications for creditors

Amendments to the CIT Act introduce the possibility for the creditor to reduce the tax base by the value of claims included in receivables for payment of a cash benefit which have not been settled or disposed of. The reduction should be made in the tax return submitted for the tax year in which 90 days have elapsed from the date of expiry of the payment deadline specified in the contract or on the invoice (bill).

If the value of the reduction in the tax base is higher than this base, the reduction of the tax base by an uncounted value shall be made in subsequent tax years, not longer than for a period of 3 years from the end of the tax year for which the right to reduction arose.

The new regulations make it possible to reduce the value of unpaid debts, the value of income constituting the basis for calculating income tax advances starting from the settlement period in which 90 days have elapsed from the date of expiry of the payment deadline to the period in which the debt was settled or sold. If the value of the income underlying the calculation of advances is higher than this income, the reduction by the uncounted value is made in the subsequent accounting periods of the tax year for which the right to reduction arose (unless the claim has been settled or disposed of).

However, if in a given year the taxpayer incurred a loss in the source of revenue with which the commercial transaction was related, the Act introduces the possibility of increasing this loss by the value of the claim included in the revenue (in the tax return filed for the tax year in which 90 days have elapsed from the date of expiry of the payment deadline).

The right to reduce the tax base or increase the loss is due if the debt has not been settled or disposed of by the date of submitting the tax return.

Receivables deducted from the tax base or increasing the amount of the loss cannot be included in tax deductible costs under other provisions of the CIT Act. At the same time, the creditor may not make the above adjustment to the tax base or the amount of the loss if, under other provisions, the claims were included in tax deductible costs (e.g. through write-offs).

In a situation where, after adjusting the tax base, the amount receivable has been settled (disposed of), the creditor will be required to increase the tax base in the settlement for the period in which such an event occurred.

Implications for debtors

The Act also introduces the obligation to increase the tax base of the debtor by the value of an unpaid monetary liability included in the tax deductible costs. Also in this case, the increase is made in the tax return for the tax year in which 90 days have elapsed since the date of payment.

At the same time, the debtor's income, which is the basis for calculating income tax advances, starting from the settlement period in which 90 days have elapsed from the date of expiry of the payment period to the period in which the liability was settled, should be increased by the value of the unpaid monetary liability.

If the taxpayer suffers a loss in a given year in the source to which the commercial transaction was related, the Act introduces the obligation to reduce it by the value of the unpaid liability included in tax deductible costs (in the tax return filed for the tax year in which 90 days have elapsed from expiry of the payment deadline). If the value of the liability exceeds the amount of the loss to be reduced, the difference increases the tax base.

The tax base must be increased (or the loss reduced) if the liability has not been settled by the date of submitting the tax return. However, if the liability is settled, the debtor has the right to make a return adjustment in the settlement for the period in which the liability will be settled.

Conditions for applying the adjustment

Regulations regarding the adjustment of the tax base or loss will apply only to claims or obligations relating to cash benefits arising in connection with commercial transactions, if the revenues or costs of obtaining them are determined at least on one of the parties (regardless of the date of their recognition). According to the example cited in the explanatory memorandum to the draft Act, in the case of acquisition of a fixed asset on which the taxpayer makes depreciation write-offs for 3 years, the adjustment of the tax base depends only on the date of payment for the contractor for this fixed asset, and not on the depreciation period.

As in the case of the solutions in force under the provisions on VAT, the Act introduces additional conditions entitling to make the adjustment of the tax base or the value of the loss, i.e.:

(i) no restructuring proceedings, insolvency or liquidation against the debtor on the last day of the month preceding the day of submitting the tax return;

(ii) a specified period from the invoice issue or the conclusion of the contract documenting the claim (generally 2 years from the end of the calendar year until the date of adjustment); and

(iii) conducting a commercial transaction as part of the creditor's and the debtor's operations, the income of which is subject to income tax on the territory of the Republic of Poland.

The Act also allows the application of new provisions in the event of settlement (disposal) of a part of a given claim.

The new regulations introduce the obligation to include in the tax returns claims or liabilities that increase or decrease the tax base (a similar solution applies to VAT).

The discussed provisions will not apply to transactions between related entities within the meaning of the provisions of the CIT Act, as, in line with the explanatory memorandum to the draft Act, there are no problems related to payment arrears in relations between related entities.

At the same time, if the payment term is set in violation of the provisions of the Payment Terms in Commercial Transactions Act, the payment term shall be understood as the term determined in accordance with the provisions of this Act.

Amendments in other acts

The provisions of the Act presume, in particular, increasing payment discipline and strengthening the legal protection of micro, small and medium-sized enterprises. Thus, the key changes relate to the regulations contained in the Act on payment deadlines in commercial transactions. The Act assumes, among others, shortening the payment deadlines in commercial transactions in which the debtor is a public entity (excluding medicinal entities) to a maximum of 30 days, while the payment deadline in transactions in which the debtor is a large entrepreneur and the creditor is a micro, small or medium entrepreneur cannot exceed 60 days (the contractual clause specifying a longer period will be invalid). The changes also include an increase in the rate of interest for delay in commercial transactions, generally by 2 percentage points. In addition, the new regulations oblige the largest CIT taxpayers to provide the Minister of Economy (currently the Minister of Entrepreneurship and Technology) with reports on payment terms used in a given year.

Entry into force

Most of the provisions of the Act will enter into force on 1 January 2020.

If you are interested in discussing the impact of the above regulations on your or your company's situation, please contact us.

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