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Tax Alert

KPMG in Poland

November 2020

Protocol amending the treaty with the Kingdom of the Netherlands on the avoidance of double taxation

On 29 October 2020 the protocol (Protocol) amending the Convention between the Republic of Poland and the Kingdom of the Netherlands on the avoidance of double taxation and the prevention of fiscal evasion with respect to taxes on income (Convention) was signed.

The Protocol takes into account the tax policy of Poland and the achievements of the OECD BEPS (Base Erosion and Profit Shifting), including proposals for tightening the tax system and combating tax fraud.

Below we present the most important amendments between the current wording of the Convention on the avoidance of double taxation concluded between Poland and the Kingdom of the Netherlands, and the Protocol.

Real estate clause

Introduction of the so-called real estate clause is one of the most important changes in relation to the current wording of the Convention.

According to this clause, gains derived by a person having a place of residence or a seat within the territory of one state from the alienation of shares or comparable rights (such as rights in a partnership or trust) may be taxed in the other state, if at any time during the 365 days preceding the alienation of these shares or comparable rights, their value derived directly or indirectly in more than 75 percent from immovable property situated on the territory of that other state.

The entry of clause into force will result in taxation of the alienation of shares or comparable rights (such as rights in a partnership or trust) if their value derived directly or indirectly in more than 75 percent during the 365 days preceding the alienation from immovable property in the country where the property is located.

Principle purpose test and a preamble

The Protocol also introduces a so-called principle purpose test, which serves as an anti-abusive clause preventing abuse of agreements on the avoidance of double taxation.

The essence of the principle purpose test is that no favourable provisions of a tax treaty may be relied on, in a situation when obtaining the treaty benefit was one of the principal purposes of a given transaction.

The test application may for example result in, the obligation to collect withholding tax on payments made by Polish residents to entities based in the Netherlands at the domestic rates (excluding rates or exemptions provided for in the Convention), if in the given circumstances the application of the provisions of the Convention is deemed by the tax authorities as an abuse of its provisions.

Importantly, a preamble will also be introduced with the Protocol, under which the Convention is concluded to eliminate double taxation, without creating the possibility of non-taxation or reduced taxation through tax evasion or tax avoidance.

Changes concerning permanent establishment

The Protocol also introduces amendments to the definition of permanent establishment.

The catalogue of exemplary activities included in the Convention, which are not covered within the meaning of permanent establishment, has been clarified by indicating that all exemplary activities indicated in the Convention (such as the use of facilities solely for the purpose of storage, display or delivery of goods or goods of enterprises) must be of auxiliary or preparatory nature in order not to result in constituting the permanent establishment.

The Protocol also stipulates that the permanent establishment will be created in a situation when a person acts on behalf of an enterprise in one of the states and by undertaking these actions concludes contracts or habitually exercises a major role in concluding contracts without significant changes made by the enterprise, and these contracts are concluded:

- on behalf of that enterprise, or
- for the transfer of the ownership, or for granting the right to use property owned by that enterprise or that the enterprise has the right to use, or
- for the provision of services by that enterprise.

According to the Protocol, the profits attributable to the permanent establishment are the profits that could have been earned, by the permanent establishment

in transactions with other parts of that enterprise, if the permanent establishment was a self-sufficient and independent enterprise engaged in similar activity under the same or similar conditions, having regard to the resources involved and the risks borne by the enterprise, establishment and other parts of the enterprise.

Recognized Pension Fund

The Protocol also introduces a definition of a recognized pension fund, indicating that it is an entity or a structure recognized as a pension fund under the law of the state of establishment which, inter alia, has been created and operates exclusively or close to exclusively to administer or provide pensions and supplementary benefits, or has been created and operates exclusively or close to exclusively to invest funds in such entities.

In accordance with the Protocol, dividends and interest will not be taxed if a recognized pension fund is a beneficiary of such a payment. Furthermore, profits from the alienation of shares, in accordance with the real estate clause described above, by such a recognised pension fund will not be taxed in the state where the real estate property is located.

Other changes

The Protocol also specifies that revenue obtained by or via an entity or structure that is fully or partially considered as tax transparent under the tax law of one of the contracting states will be considered as revenue of a person having residency or seat within the territory of a given state to the extent that this revenue for the purposes of taxation by that state is treated as revenue of a person having residency or seat within the territory of that state (transparent entity clause).

The Protocol also modifies the principle under which, when a legal person has its seat within the territory of two states, it is considered to have its seat in the state of its effective management. In such a situation, states will undertake actions aimed at determining the state of seat in the course of mutual arbitration. If no agreement is reached, the person will not be entitled to any tax relief or exemption under the Convention.

The Protocol also specifies the rules of applying the procedure of mutual arbitration and information exchange.

Additionally, the Protocol introduces the principle that revenue obtained in connection with the company liquidation or acquisition of own shares by a company is treated as shares derived revenue. Revenue derived in connection with distributions on certificates or participation units of investment funds will be treated similarly.

Protocol and the change of the method of avoiding double taxation

Contrary to previous announcements, the Protocol will not change the avoidance of double taxation method applied by Poland to its tax residents deriving income in the Netherlands (the proportional tax credit method will be continued). Consequently, Polish tax residents deriving income in the Netherlands will still be entitled to the abolition relief on the basis of the principles referred to in the provisions of the Personal Income Tax Act, however, these rules may be subject to change.

What next?

The Protocol signed by representatives of the Polish and Dutch tax authorities is available on the website of the Ministry of Foreign Affairs.

The Protocol must be ratified by Poland and the Netherlands to come into force.

The Protocol will enter into force at the end of the third month following the month of the mutual notification that both contracting states fulfilled their constitutional conditions for its application and will apply to tax years, periods and taxable events taking place on the first day or after the first January of the calendar year following the year in which the Protocol entered into force, i.e. no earlier than on 1 January 2022.

If you would like our assistance, please contact us at: mampytanie@kpmg.pl

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