

On 24 November 2008 the President signed the act of 6 November 2008 amending the Personal Income Tax Act, the Corporate Income Tax Act and also some other acts („the Act”). Among others, the Act introduces new regulations concerning transfer pricing issues. These new regulations will allow taxpayers to eliminate double taxation in transactions concluded with their foreign related parties. The Act will come into force on 1 January 2009.

The scope of the new regulations

The new regulations will concern entities which are seated in Poland and conclude transactions with their foreign related parties. According to the Act, a taxpayer will be eligible to apply for having its income adjusted if the income in question was also taxed abroad as income of the Polish taxpayer's foreign related party.

Implementation of the new regulations is linked to the fact that Poland joined the so-called *Arbitration Convention (90/436/EEC)* which is in force in EU countries. The *Arbitration Convention* introduced the possibility of applying for an adjustment of the income of a Polish entity in cases where the tax authorities of another EU country assessed additional income to its foreign related party. One of the achievements of the *Arbitration Convention* is an obligation for participant countries to reach final agreement concerning the amount of adjustment. The tax authorities of both countries are obliged to reach a consensus concerning the arm's length level of pricing in a given

transaction. This consensus should also indicate the level of potential income to be additionally assessed as well as the level of potential adjustment to be made.

The Ministry of Finance is currently working on a draft of a decree, which will define the manner and procedure of applying for the adjustment. In this matter the present version of the decree refers directly to the *Arbitration Convention*, which binds only EU countries. However, according to the justification of the Act it is planned that the rules set out in the decree will apply also to the procedures of mutual agreement incorporated in the double taxation agreements

Profit adjustment application procedure

According to the draft of the decree, in order to obtain an adjustment of income, the taxpayer will have to file a formal application for the Ministry of Finance. The application should include, among others, the following elements: copies of tax assessment notices (decisions), a tax audit report

or a document equivalent to it, stating that the alleged double taxation actually took place as well as the taxpayer's stance regarding the correctness of the arm's length methods applied. Moreover it has to be pointed out that the taxpayer cannot apply for the tax adjustment if three years has passed since the day when the taxpayer received his first tax assessment notice resulting in double taxation.

According to *the Convention*, during stage I of the procedure, the tax authorities of the two countries are obliged to conduct negotiations and are supposed to reach an agreement within two years - the same period of time is indicated in the draft of decree. If, after two years the countries will not have reached an agreement, then an Arbitration committee will be appointed (stage II of the procedure). The opinion of the Arbitration committee will be binding for the tax authorities of the countries in question. Stage II of the procedure, however, was not included in the draft of the decree. Therefore it seems that in this case resolutions of the *Arbitration Convention* will be binding.

Time frame

The resolutions of the Act will come into force on 1 January 2009. However it has to be pointed out that taxpayers are allowed to apply for the adjustment of their income based on the *Arbitration Convention* which is already binding in all EU countries (in Poland since 1 February 2007).

Advantages for taxpayers

The amendment discussed, as well as the *Arbitration Convention* regulates the rules of conducting the agreement and arbitration procedures under Polish tax law. It can be also perceived as a new tool which can be used in order to manage transfer pricing risk. This will allow Polish taxpayers to obtain a tax refund in cases where a foreign contracting party of a given entity (seated in one of the EU countries) had income additionally assessed and was charged with additional tax by the tax authorities of the country in question.

It has to be borne in mind that the *Arbitration Convention*, unlike the mutual agreement procedure, obliges EU countries to reach an agreement in terms of the adjustments to be made. The *Arbitration Convention* has already been used in practice in order to eliminate double taxation in some cases of transactions concluded between the EU countries' taxpayers.

If you are interested in discussing the above mentioned issue in more detail, obtaining more information concerning the amendments introduced or obtaining another consultation concerning transactions concluded with related parties, please do not hesitate to contact the Transfer Pricing Team of KPMG Tax M. Michna Sp. k.

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