

Tax alert

Tax services

New Poland-Norway Double Tax Convention

Signed in Warsaw by the Ministers of Foreign Affairs of Poland and Norway on 9 September 2009, the new Convention for the Avoidance of Double Taxation and the Prevention of Fiscal Evasion with Respect to Taxes on Income has replaced the existing treaty signed in Oslo on 24 May 1977.

The new convention introduces a number of important changes in the taxation of incomes earned in Poland by Norwegian entities (and, vice versa, those earned by Polish entities in Norway). We provide a brief summary of the key changes.

Definition of a permanent establishment extended

The definition of a permanent establishment has been extended to include an activity involving the supply of services by an enterprise of a Contracting State which provides services in the other Contracting State:

- (I) through an individual who is present in that other State during a period or periods exceeding in the aggregate 183 days in any 12-month period; or
- (II) during a period or periods exceeding in the aggregate 183 days in any 12-month period, and these services are performed for the same project or connected projects through one or more individuals who are performing such services in that other State or are present in that State for the purpose of performing such services.

and more than 50% of the gross revenues attributable to the business activities of the enterprise during this period or periods are derived from services in that other State through those individuals.

This part of the definition of a permanent establishment is a new concept not known from any of Poland's double tax treaties signed so far.



Lukasz Ziólek
Partner
phone: +48 22 557 7545
e-mail: Lukasz.Ziolek@pl.ey.com



Tomasz Krasowski
Manager
phone: +48 22 557 7831
e-mail: Tomasz.Krasowski@pl.ey.com

The practical implication of the extended definition of a permanent establishment is that more Norwegian enterprises carrying on a business activity in Poland (in a manner giving rise to a permanent establishment) will be liable to report and pay tax on income from that business in Poland (and, analogously, more Polish enterprises will report and pay tax in Norway).

The new convention also defines activities which are carried on offshore in a Contracting State in connection with the exploration or exploitation of the seabed and subsoil and their natural resources situated in that State. An activity thus defined carried on by an enterprise of a Contracting State will be deemed to be carried on through a permanent establishment situated in that other State already when the period or periods of carrying on offshore activities exceed 30 days in the aggregate in any 12-month period commencing or ending in the fiscal year concerned.

Please note that under the new convention a building site, a construction, an assembly or installation project will qualify as a permanent establishment of an enterprise in the source country if they last for a period of more than 12 months (the existing "old" treaty sets a more favourable period of 18 months).

„Beneficial owner” clause

Introduced in the clauses of the new convention governing the taxation of dividends, interest and royalties is the concept of a "beneficial owner". This clause restricts the applicability of the preferential withholding tax rate under the convention to the sums paid to their actual economical owner. This means that the preferential withholding tax rate will not be available to entities which, although being residents of the other State, are not beneficial owners but merely intermediaries whose task is to transfer a sum to another entity. This restriction is in line with Poland's overall direction in negotiating double tax treaties.

Withholding tax exemption for dividends

The new convention applies a withholding tax exemption for dividends paid to a company established in the other Contracting State if the company holds directly at least 10% of the capital of the company paying the dividends on the date when the dividends are paid and has done so or will have done so for an uninterrupted period of 24 months in which the payment was made. This exemption will replace the existing 5% withholding tax rate, which is available to shareholders holding at least 25% of the company paying the dividends. This change is designed merely to clarify the existing legal system and ensure harmonisation of treaty provisions with the taxation of dividends set out in Directive 90/435/EEC on the common system of taxation applicable in the case of parent companies and subsidiaries of different Member States, which also applies to Norway under the European Economic Area Agreement. The directive has already been implemented in the Polish legal system (Article 20 and Article 22 of the CIT Act) and also applies to dividends transferred between enterprises established in Poland and in Norway.

Exemption for interest cancelled

Unlike the existing treaty, which exempts interest in the source country from withholding tax if that interest is paid to a resident of the other State, the new convention introduces a 5% withholding tax on interest; this confirms the direction followed in the new treaties signed by Poland. The change shows the need to analyse the effectiveness of debt-financing schemes given the new withholding tax rate and to consider restructuring such schemes.

Notwithstanding, the exemption will continue to apply to e.g. interest on bank loans.

Ernst & Young

Assurance | Tax | Transactions | Advisory

Ernst & Young is a global leader in assurance, tax, transaction and advisory services. Worldwide, our 144,000 people are united by our shared values and an unwavering commitment to quality. We make a difference by helping our people, our clients and our wider communities achieve their potential.

For more information, please visit www.ey.com/pl

Ernst & Young
00-124 Warsaw, Rondo ONZ 1
Tel.: +48 (22) 557 70 00
Fax: +48 (22) 557 70 01

This publication has been carefully prepared but it necessarily contains information in summary form and is therefore intended for general guidance only, and is not intended to be a substitute for detailed research of the exercise of professional judgment. Ernst & Young can accept no responsibility for loss occasioned to any person acting or refraining from action as a result of any material in this publication. On any specific matter, reference should be made to the appropriate advisor.

© 2009 Ernst & Young
All Rights Reserved.
Ernst & Young refers to the global organization of member firms of Ernst & Young Global Limited, each of which is a separate legal entity. Ernst & Young Global Limited, a UK company limited by guarantee, does not provide services to clients.

SCORE No: 004.11.09

Lower withholding tax rate on royalties

Once the new convention takes effect, the existing 10% withholding tax rate on royalties will be replaced with a lower rate of 5%. Under the new treaty, royalties also include any payments related to cinematograph films as well as films or tapes for radio or television broadcasting.

Real estate clause

The new convention introduces the so-called "real estate clause" in the section governing taxation of capital gains. Under the clause, gains from a transfer (alienation) of shares which derive more than 50% of their value directly or indirectly from immovable property are taxable in the state where the property is situated. With this change, a Norwegian company's transfer of shares in a company key asset of which is immovable property situated in Poland (or shares in another company whose key asset is such property) will also be taxable in Poland (under the existing treaty it is taxable in Norway only). This change is of key importance to Norwegian enterprises holding shares in Polish real property or development vehicle companies.

Taxation of income from employment in the source country

The new convention sets out more stringent conditions for taxation of income from employment exercised in the other State only in the country where the employee is resident. In addition to the requirements applicable under the 1977 Convention, the recipient of employment income must also fulfil the following conditions to benefit from the tax exemption in the country where his employment is exercised:

- (I) the recipient is present in that state for a period or periods not exceeding in the aggregate 183 days in any 12-month period commencing or ending in the tax year concerned (not 183 days in a given financial year as under the existing treaty); and
- (II) the employment is not a case of hiring out of labour.

All the conditions set out above should be met at the same time, otherwise employment income will be taxable both in the state where the employment is exercised and the state where the recipient is resident (considering the relevant method of avoiding double tax).

The change requires that the circumstances determining the fulfilment of the conditions for the exemption be examined for each employee seconded to/ from another country.

Effective date

The new convention is already available on the Ministry of Finance web site but it will not take effect until after each state has ratified it within the applicable procedure (in Poland the convention is to be ratified by the President with Parliament's approval expressed in a statute). Technically, the convention will come into force once the two Contracting States exchange the diplomatic notes concerning the ratification; however, as a rule it will apply to incomes earned from 1 January of the year following the year in which it becomes effective.

If you have any questions concerning the new Poland-Norway Double Tax Convention, please feel free to contact us.

Łukasz Ziółek

Tomasz Krasowski