TAX BENEFITS OF ADOPTING A RESOLUTION ON LEAVING A PROFIT IN A COMPANY WHICH IS A CIT TAXPAYER

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Due to the upcoming period of holding the Ordinary Shareholders' Meetings for 2020 it is worth remembering that the legal regulations make it possible to recognize the so-called hypothetical interest cost on equity (allowance for corporate equity – ACE) as tax deductible expenses. This solution concerns additional contributions and profits excluded from the distribution and transferred to the company's reserve or supplementary capital. According to the Article 15cb sec. 1 of the Act of 15.02.1992 on Corporate Income Tax (hereinafter: 'CIT Act'), in force since 2019, tax deductible expenses shall also include an amount corresponding to the product of the reference rate of the National Bank of Poland applicable on the last working day of the year preceding the fiscal year increased by 1 percentage point and the amount of:

1. an additional contribution made to the company in accordance with the procedure and the rules set out in separate regulations or

2. a profit transferred to the company's reserve capital or supplementary capital.

The above expense may be deducted in the year in which the additional contribution is made or in which the reserve or supplementary capital is increased and in the next two consecutive fiscal years, and the total amount of tax deductible expenses deducted in a fiscal year on the grounds listed in sec. 1 shall not exceed the amount of PLN 250,000 (Article 15cb sec. 2 and 3 of CIT Act).

Note:

The above expense may not be deducted in the following cases:

1. the additional contributions and profits allocated for covering a balance-sheet loss,

2. if the additional contribution is repaid or the profit is distributed and paid before the lapse of 3 years counting from the end of the fiscal year in which that contribution was made to the company or in which the resolution on the retention of the profit in the company was adopted,

3. if the additional contribution or exclusion from the profit distribution and its transfer to the reserve or supplementary capital have been made without justified economic reasons, mainly for the purpose of recognizing the above amount of hypothetical interest cost as a tax deductible expense. Justified economic reasons do not include cases where a benefit earned in a tax year or subsequent years arises from recognition as tax deductible expenses.

As a general rule, the moment of making the additional contribution/increasing the reserve capital or supplementary capital is considered the moment of settling the above expense. However, in accordance with the Article 10 sec. 1 of the amending Act (i.e. the Act of 23.10.2018 amending the Act on Personal Income Tax, the Act on Corporate Income Tax and certain other acts, which introduced the above Article 15cb):

- Article 15cb shall apply for the first time to the tax year commenced after 31.12.2019.
- Article 15cb shall also apply to additional contributions made and profits transferred to reserve or supplementary capital after 31.12.2018.

This means that the company's profit earned in 2018, which was transferred to the supplementary capital in 2019, should be treated as the profit transferred to the supplementary capital in 2020, and the interest related to that transferred profit may be recognized as tax deductible expenses for 2020, 2021 and 2022 (in accordance with the abovementioned Article 15cb sec. 2 of CIT Act).

In the following years, there is a mechanism that no longer raises any doubts and according to which the expense may be deducted in the year of making an additional contribution or increasing the reserve or supplementary capital and in the next two consecutive fiscal years, and the total amount of tax deductible expenses deducted in the fiscal year on the grounds listed in sec. 1 shall not exceed the amount of PLN 250,000.

Should you have further questions, we remain at your disposal.

* This Newsletter does not constitute legal or tax advice.