CLIFFORD CHANCE

Client briefing
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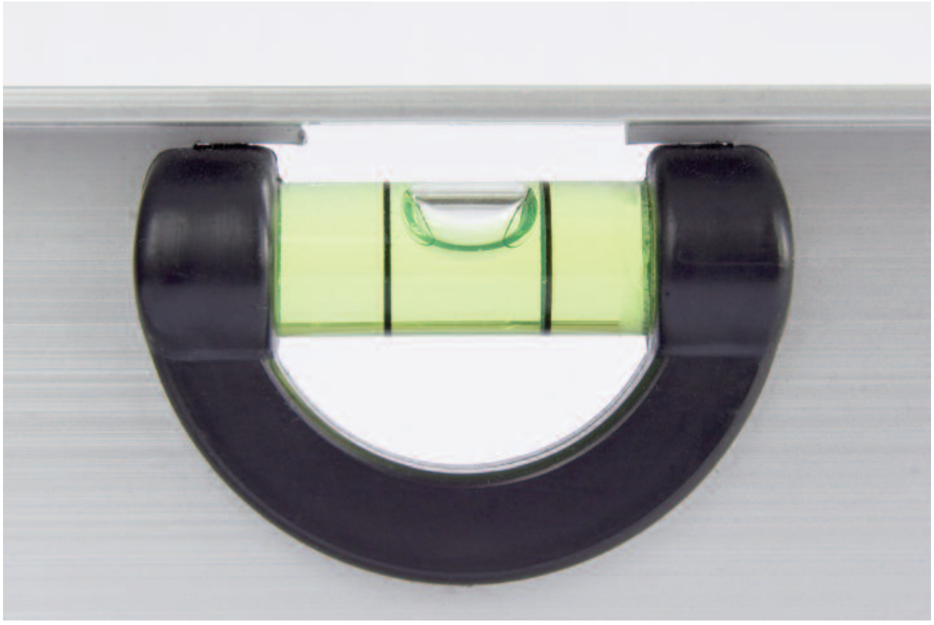
Withholding tax on interest and taxation of funds



Key Issues

The content of this Client Briefing may be good news for European investment and pension funds interested in lending to Polish companies.

On 1 January 2011, an amendment to the Corporate Income Tax Act will come into force, expanding a tax exemption to include the income of investment funds and pension funds with their seats in the countries of the European Union and European Economic Area ("EEA"). This exemption will also apply to withholding tax on revenue (income) paid out to those funds, including interest on the funds' receivables from Polish entities.

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General regulation

In general, payments of interest on borrowed funds by a Polish entity to a non-resident legal person are subject to Polish withholding tax at the rate of 20%, subject to reduction or exemption pursuant to the terms of an applicable double tax treaty.

According to the Polish regulations which implement the EU Interest & Royalties Directive of 3 June 2003, an additional specific rate or exemption from withholding tax on interest may also apply. In the event that interest payments are made by an entity having its registered seat in Poland to a foreign entity having its registered seat in one of the EU or EEA member states, the rate of income tax which must be collected in Poland, amounts to:

1) from 1 July 2009 to 30 June 2013 – 5%,

2) from 1 July 2013 these payments will be exempt from taxation.

However, this rate of withholding tax in Poland (or exemption from taxation) will apply only if all the following conditions in the form binding from 1 January 2011 are met (otherwise the rate of tax will be 20%):

1) the interest is paid out by:

   a) a company that is an income tax payer with its registered office or management board in Poland; or
   b) a foreign establishment situated in Poland, of a company subject to corporate income tax in an EU member state on all of its income irrespective of where earned, if the amounts paid by the foreign establishment are subject to qualification as revenue-earning costs when determining its taxable income in Poland;

2) the entity receiving the interest is a company subject to taxation on all its income, irrespective of where earned, in an EU and EEA member state other than Poland;

3) the company:

   a) referred to in point 1 directly owns no less than 25% of the shares in the capital of the company referred to in point 2, or
   b) referred to in point 2 directly owns no less than 25% of the shares in the capital of the company referred to in point 1, or
   c) referred to in point 2 shall not benefit from an exemption from income tax on its total income, irrespective of where that income is achieved;

4) the recipient of the interest is:

   a) a company referred to in point 2, or
   b) a foreign establishment of a company referred to in point 2, if the income earned as a result of obtaining those amounts is subject to taxation in the EU member state in which the foreign establishment is located.

The condition of possessing shares referred to in point 3 shall also be regarded as fulfilled providing that another company which is subject to income tax on its total income in an EU or EEA member state, irrespective of the place where such income is achieved, directly owns - not less than 25% of the shares both in the share capital of the company referred to in point 1 as well as the share capital of the company referred to in point 2.

The decreased rate of tax (and exemptions from 1 July 2013) applies if the companies referred to in point 3 own shares in the amount referred to in point 3 continuously for two years. However, the period in which such exemptions apply may also elapse after the date on which the company referred to in point 2 receives the interest.

Double tax treaties

According to double tax treaties and local Polish regulations, withholding tax rates are usually reduced to 10% or 5% or exempt from withholding tax on the following conditions:

1) The lender provides the borrower with a certificate of tax residency issued by the relevant tax authorities, presenting the tax residency of the lender as at the time of the given interest payment.

2) Pursuant to double tax treaties, the amount of interest does not exceed the amount which would have been agreed on between independent enterprises (the arm's-length principle).

3) The lender is not covered by the Limitation of Benefits clause (i.e. the provisions which affect the rules of the treaty which exclude or limit taxation in the state of source) – if provided for by a relevant double tax treaty.

4) The lender passes the beneficial owner test – if a relevant double tax treaty requires the lender to be the beneficial owner of the interest.

Under many double tax treaties interest on bank loans is exempt from withholding tax. (Please see withholding tax matrix attached.)

Regulations on investment & pension funds

Currently Polish regulated investment and pension funds exempt from corporate income tax (CIT). According to an amendment to the CIT Act that will to take effect as of 1 January 2011, foreign investment funds and foreign pension funds will also be exempt from CIT.

The exemption for investment funds is contingent on the fulfilment by the relevant institutions of all of the following conditions:

1) they are subject, in the Member State in which they have their registered seat, to income tax on all their income, notwithstanding the place of its generation,

2) the sole object of their activity is the collective investment of cash gathered through public and non-public offers to acquire their participation units in securities, money market instruments and other proprietary rights,

3) they carry out their activity on the basis of a permit issued by the relevant authorities of the Member State in which they have their registered seat,

4) their activity is subject to supervision by the relevant authorities of the Member State in which they have their registered seat, and

5) they have a depositary who acts as a custodian of the assets of that institution.

The exemption from taxation for pension funds is contingent on the fulfilment by these institutions of all of the following conditions:

1) they are subject, in the Member State in which they have their registered seat, to income tax on all their income, notwithstanding the place of its generation,

2) they carry out their activity on the basis of a permit issued by the relevant authorities of the Member State in which they have their registered seat,

3) their activity is subject to supervision of the relevant authorities of the Member State in which they have their registered seat,

4) they have a depositary who keeps a register of the assets of that institution, and

5) the sole object of their activity is gathering cash, and its investment for the purposes of payments in favour of participants of a pension programme after they reach retirement age.

Taking into consideration the above conditions, foreign investment and pension funds operating according to rules which are similar to those applying to Polish investment and pension funds will be exempt from corporate income tax. **The exemption from corporate income tax also means that payments made to such foreign investment and pension funds will not be subject to withholding tax in Poland.**

A condition for exemption from corporate income tax is that there is a legal basis upon which the Polish tax authorities can obtain tax information by the tax authorities from the tax authorities in the Member State in which such investment or pension fund has its registered seat. The basis upon which the Polish tax authorities may carry this out are:

1) the provisions implementing Council Directive of 19 December 1977 concerning mutual assistance by competent authorities of Member States in the field of direct taxation and taxation of insurance premiums,

2) the provisions of the Convention on mutual administrative assistance in tax matters, of 25 January 1988, and

3) the provisions of any double taxation treaty concluded between Poland and the Member State in which the foreign investment or pension fund has its registered seat.

Attachment

The following table summarises Polish withholding tax rates on interest applied under the provisions of various double tax treaties.

No.	The country	Withholding tax on interest – standard treaty rates (%)	Withholding tax on interest – treaty rates on bank loans (%)
1	Albania	10	10
2	Australia	10	10
3	Austria	5	0
4	Belarus	10	10
5	Belgium	5	0
6	Bulgaria	10	10
7	Canada	15	15
8	China (PRC)	10	10
9	Croatia	10	10
10	Cyprus	10	10
11	Czech Republic	10	10
12	Denmark	5	5
13	Estonia	10	10
14	Finland	5 from 1 January 2011; 0% until 31 December 2010	0
15	France	0 (will be renegotiated)	0
16	Germany	5	0
17	Greece	10	10
18	Holland	5	0
19	Hungary	10	10
20	Iceland	10	10
21	India	15	15
22	Indonesia	10	10
23	Ireland	10	0
24	Israel	5	5
25	Italy	10	10
26	Japan	10	10
27	Jordan	10	10
28	Kazakhstan	10	10
29	Korea	10	10

No.	The country	Withholding tax on interest – standard treaty rates (%)	Withholding tax on interest – treaty rates on bank loans (%)
29	Korea	10	10
30	Latvia	10	10
31	Lithuania	10	10
32	Luxembourg	10	0
33	Malaysia	15	15
34	Malta	10	10
35	Morocco	10	10
36	Moldavia	10	10
37	Norway	0 from 1 January 2011; 0% until 31 December 2010	5
38	Philippines	10	10
39	Portugal	10	10
40	Republic of South Africa	10	10
41	Romania	10	10
42	Russia	10	10
43	Singapore	10	10
44	Slovakia	10	10
45	Slovenia	10	10
46	Spain	0	0
47	Sri Lanka	10	0
48	Sweden	0	0
49	Switzerland	10	10
50	Thailand	10	10
51	Tunisia	12	12
52	Turkey	10	10
53	Ukraine	10	10
54	United Kingdom	5	0
55	USA	0 (under renegotiations)	0
56	Uzbekistan	10	10
57	United Arab Emirates	5	5
58	Vietnam	10	10
59	Yugoslavia	10	10
60	Zimbabwe	10	10