KSP TAX NEWS 02/2013

We are pleased to present to you KSP Tax News, in which we describe selected judgments and interpretations issued or published in January 2013. We hope this publication proves useful in your everyday operation.

Taxation of leasing insurance service – judgment of the Court of Justice of the European Union

The Court of Justice of the European Union (CJEU) in the judgment of 17 January 2013, file C-224/11, resolved that the service of insuring of an object of leasing cannot be considered as an ancillary service subject to VAT according to the rules applicable to the principle service, i.e. leasing.
The case considered by CJEU concerned a lease agreement under which a lessee is obliged to insure the leased items. The lessee could purchase the insurance service by himself or use the offer of the lessor who was concluding an agreement with the insurance company and afterwards re-invoiced the cost to the lessee. In such a situation, according to the company, it was providing two independent services: leasing and insurance. As a consequence, the leasing service was subject to the basic VAT rate and the insurance service was exempted from taxation. Such a procedure was questioned by tax authorities pursuant to which the service of insuring was of ancillary nature with regard to the leasing service, thus the insurance service should be subject to taxation, just as the main service. However, CJEU decided that the abovementioned services cannot be considered as a comprehensive service, due to the fact that the insurance of a leased item does not provide for a better use of the leasing service, but it constitutes the objectives for the lessee per se. What is more, the condition laid down by the lessor also did not prejudge the above because the user could freely choose the insurer. Moreover, CJEU stated that the activity consisting in conclusion of an insurance agreement by the lessor and re-invoicing of its costs to the lessee who was using this protection, is exempted from taxation as an insurance transaction. Nevertheless, it should be pointed out that the above refers to the situation where the service of insuring remains unchanged in its shape and the lessor re-invoices the cost without any margin

Expert comment

„The decision of CJEU may prove to be helpful in disputes between lessors and tax authorities as regards the method of taxation of a service consisting in insurance of a leased item pursuant to the VAT Act. This judgment is of vital importance for the entire leasing industry. It specifies that the current practice of tax authorities as regards application of the same VAT rules both to the services of leasing and insuring is incorrect. The issue of taxation of the insurance of a leased item has already been discussed before the Supreme Administrative Court (NSA). Nonetheless, the NSA composed of 7 judges denied the leasing companies, in its judgment of 8 November 2010 (I FPS 3/10), the right to apply

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the exemption with regard to the insurance service re-invoiced along with the leasing agreement. The above-mentioned resolution confirmed to some extent the previous (unfavourable for taxpayers) practice of tax authorities and administrative courts.

In contrast to the aforesaid resolution, CJEU specified in the decision that the service of insuring the leased item insurance and the leasing service, as a rule, are separate services and do not depend on the VAT purposes. However, it is the administrative courts that should determine whether particular actions in a given case are as much related to each other that they should be regarded as a single service or on the contrary – they are separate services. When the lessor insures the leased item and charges the lessee with the exact cost of insurance, this action is regarded as an insurance transaction and therefore it should be exempted from taxation under VAT Act regulations. The subject decision should end the questioning by tax authorities of settlements of the taxpayers who applies exemption from VAT with regard to the re-invoiced insurance in lease agreements.

What is more, the commented decision of CJEU may constitute the basis for challenging the negative decisions issued by tax authorities as a result of misinterpretation of regulations or individual interpretations. However, it may allow the taxpayers to receive the previously overpaid VAT. The request within that scope may be filed within one month from the date of publication of the decision in the Office Journal of the European Union. At the same time, we should take into consideration the risk of challenging, by the tax authorities, the VAT deductions from the service of insuring the leased item, if this service is to be subject to VAT exemption under the CJEU decision".

CIT

The Supreme Administrative Court in the judgment of 30 January 2013 (II FSK 1216/11) decided that in order to verify whether there is a so-called thin capitalization, the amount of the debt due to the so-called significant shareholders should be calculated as of the date of payment of interest.
In the presented case, the company received a loan from the so-called significant shareholders holding at least 25% of shares. In such a situation, according to Article 16 point 1 item 60 and 61 of the CIT Act, if the amount of the debt towards those shareholders exceeds triple the amount of the share capital, the interest on the loan does not constitute tax deductible expenses in the part that reaches triple the amount of the share capital. However, in the subject case, after the principal amount of the loan had been paid, the shareholder sold the liabilities including the due interest to the entity unrelated to the company. In this situation, according to the company, it may include the interest to the tax deductible costs because as of the date of their repayment, it will not exceed the debt limit referred to in Article 16 point 1 item 60 and 61 of the CIT Act. This standpoint was found to be correct both by the court of I instance and the Supreme Administrative Court during the dispute with the tax authorities. It results from the judgments that two conditions have to be met jointly for thin capitalization: the shareholder must meet the requirement for recognizing him as the so-called significant shareholder as of the date of conclusion of the loan agreement with this shareholder and the amount of the company's debt towards all the significant shareholders cannot exceed, as of the date of payment of interest, triple the amount of the share capital of that

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company. If at least one of the abovementioned conditions is not met, all the interest can be included to the tax costs. In the presented case, the limitation within including the interest to the tax deductible costs could not be applied due to the fact that the amount of debt towards the significant shareholders had been reduced as of the date of payment of interest and thus, the second condition for thin capitalization had not been fulfilled.

The Supreme Administrative Court in the judgment of 15 January 2013 (II FSK 1052/11) confirmed that the obligation to prepare tax documentation arises if the total amount of all transaction between particular related entities exceeds the limit of EUR 30,000. The acquisition of services from third parties for the benefit of the company and re-invoicing them is also a transaction subject to the obligation of their documentation.
In the subject case, the company concluded two agreements with its shareholder. Under one of those agreements, the shareholder was obliged to provide to the company a range of services of advisory nature and under the second one, the shareholder was obliged to purchase services from third parties for the benefit of the company and re-invoice those services. Due to the fact that none of the abovementioned agreements did not exceed the limit of EUR 30,000, despite that fact that jointly they exceeded the limit, according to the company, there was no obligation to document the transactions, especially that, as far as the company was concerned, the re-invoicing is not a transaction because the shareholder cannot add a margin. The above was questioned by NSA, in the opinion of which, applying the limit to each transaction separately causes that the obligation to document is a fiction because the entrepreneurs may freely shape the prices in order to avoid that obligation . This judgment is part of a negative to the taxpayers case-law line, according to which the limits of transactions between related entities include all transactions jointly, regardless of their diverse subject. Moreover, NSA confirmed in the presented judgment that re-invoicing the services is also a transaction which should be documented.

The Province Administrative Court in Warsaw in its judgment of 23 January 2013 (III SA/Wa 1641/12) resolved that the costs related to hiring the management board, employees and having an office outside the special economic zone (SEZ) constitute eligible costs because of their ancillary nature towards the business activity in SEZ. Those costs should also be settled on the accrual basis, i.e. on the date of their accounting.
A company acting within SEZ was employing administrative staff and the management board in leased premises in Warsaw, outside the zone. The company started to have doubts whether the expenses associated with operations of its office and employees working there can be included to the zone costs. The obtained individual interpretation provided for that the activity related to hiring employees and running the office outside SEZ does not constitute zone activity and related expenses are not zone costs. Moreover, the authority issuing the interpretation was of the opinion that the costs should be recognized at the date they were incurred (paid) and not when they were accounted for in the books. However, according to the court, employment of administrative staff and the management board is necessary for running business activity within SEZ but it is of no importance that those activities are performed outside the zone. Thus, the expenses related to the existence of the seat in Warsaw are the zone costs. The court upheld also, in the subject judgment, the position favourable to the taxpayers that the zone costs should be recognized at the date of their accounting (accrual basis) and not at the date

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when they were actually incurred (cash basis). Nevertheless, an adverse opinion was presented, among others, by NSA in the judgment of 25 April 2012 (II FSK 2099/10), in which the cash basis was considered as appropriate for assigning the zone costs.

VAT

The Province Administrative Court in Poznan, in the judgment of 4 January 2013 (I SA/Po 719/12) decided that the payment of dividends in kind as a transfer of the ownership right to a real estate is subject to VAT, regardless of the fact that the real estate was to be further used in the company's business activity.

In the presented case, a limited liability company (sp. z o.o.) was considering to pay the dividend in kind by transferring the ownership right to the real estate used for the company's business activity to the shareholders. After the transfer of the real estate to the shareholders, the real estate was to be leased to the company. The tax authorities recognized that such a transaction is subject to VAT because the transfer of the real estate is made free of charge for the personal use of the shareholders. WSA agreed with the standpoint of the tax authorities. According to the court, it is of no importance whether, after the free of charge transfer, the shareholders are going to lease the real estate to the company because the transfer of the ownership right by itself meets the conditions of a transfer for personal purposes of the shareholders under the VAT Act. This judgment is a part of the taxpayers case-law line according to which, the payment of dividend in kind is treated as a supply of goods or provision of services under the VAT Act, thus it is subject to taxation.

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If you wish to be provided with additional information in this respect, please contact us:

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