

## FUNDAMENTAL AMENDMENT TO THE TERMS OF SETTLING CORPORATE INCOME TAX PROVIDED FOR IN THE DRAFT AMENDMENTS TO THE CIT ACT. TAX EFFECTIVENESS OF DEBT PUSH-DOWN THREATENED?

One of the amendments to the Corporate Income Tax Act planned by the Polish Ministry of Finance may be a turning point in the method of settling corporate income tax. Namely, the draft amendment provides for the division of revenues into two baskets, i.e. capital gains and revenues from other sources. This may come into effect on 1 January 2018.

### BACKGROUND

The draft amendment contains a list of the types of revenue that will be classified as capital gains. This list includes, inter alia:

- revenues from a share in the profits of legal persons, including:
  - dividends;
  - revenues from the redemption of shares or a decrease in their value;
  - value of assets received in connection with the liquidation of a legal person or a partnership limited by shares;
  - interest on a participation loan; and
  - revenues earned as a result of transformations, merger or de-mergers;
- other revenues from shares in a legal person or a partnership limited by shares, including:
  - revenue from the transfer of shares, including transfers for the purpose of redemption of shares; and
  - revenues earned as a result of converting shares;
- revenues in respect of a contribution in kind made to a legal person or a partnership limited by shares;
- revenues from the transfer of receivables; and
- revenues from securities and financial derivatives and also revenues from their transfer.

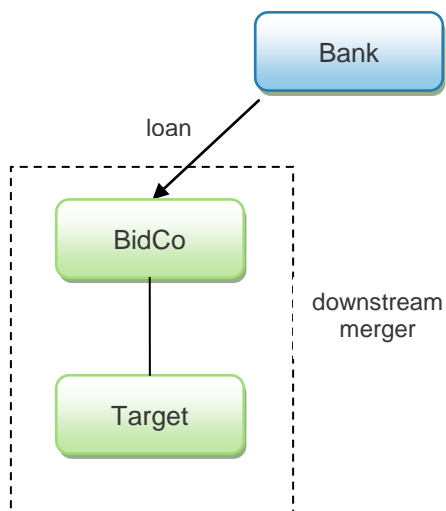
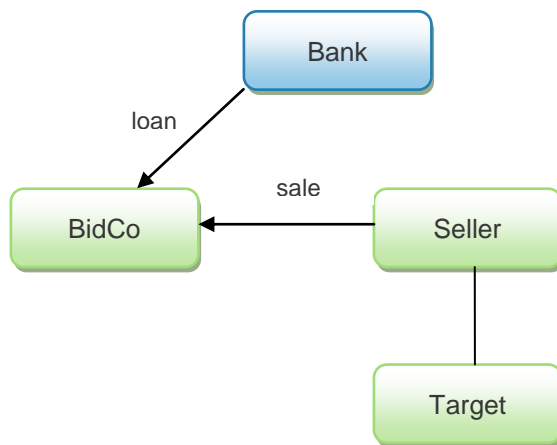
Under the draft amendment, income is determined separately for each relevant basket, i.e. revenue from capital gains is separated from revenue from other sources. Correspondingly, the tax losses will have to be determined separately for each of these baskets, whereby a tax loss from one basket may not be deducted against the income from the other basket. Within the same basket, losses can be deducted for five tax years, in an amount not exceeding 50% of the loss in any of those years.

The income and loss under each basket would be determined by adding together the revenues of the relevant basket and the costs of earning revenues from that basket. Costs that cannot be attributed to revenues from a particular basket would be attributed to the two baskets in the same ratio as the revenue earned from sources belonging to the relevant basket in the relevant tax year to the total amount of revenue in that tax year.

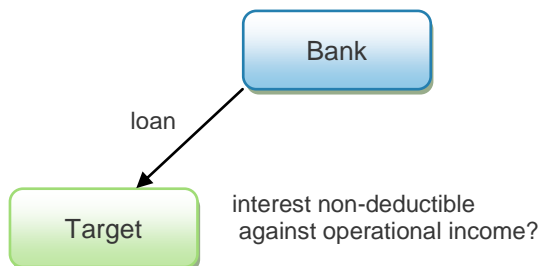
To summarise, it will not be possible to combine the costs of revenues of one basket with the costs and revenues of the other basket. Furthermore, it will not be possible to deduct any tax loss attributed to one basket against the income attributed to the second basket.

### POTENTIALLY AFFECTED STRUCTURES – DEBT PUSH-DOWN

What structures could be affected by the above-mentioned amendment? It is possible that the amendment may adversely affect e.g. debt push-down structures. They assume that interest on a loan granted to an acquiring company ("**BidCo**") to purchase shares is deducted against the operational revenue of the company shares in which are acquired ("**Target**") after it is merged with BidCo (see the diagrams below).



In this structure, there is a risk of it being assumed that interest on a loan granted to acquire shares are costs of earning revenue from those shares. Consequently, interest would be attributed to the capital gains basket. With such a classification, the right to deduct the interest on the loan to acquire the shares against the operational revenue of the Target after its merger with BidCo, could be challenged. Therefore, we will monitor and report any further developments regarding this change.



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