TAXATION OF INCOME FROM INVOLVEMENT IN PARTNERSHIPS IN POLAND

[a]AGNIESZKA SOBIECH

Poznan University of Economics and Business, Al. Niepodległości 10, 60-101 Poznań, Poland, email: [a]a.sobiech@ue.poznan.pl

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Abstract: Tax systems in different countries take various approaches to the problem of income taxation of partnerships. The Polish legislation has based the taxation of income from partnerships on aggregate theory. Consequently, income arising from involvement in a partnership is typically taxed at the level of its partners (natural or legal persons). This paper presents Polish tax regulations applicable to incomes received from partnerships.

Keywords: partnership taxation, income taxes

1 Background

The method of taxation applicable to partnerships is one of the fundamental advantages provided by the tax law to such forms of conducting economic activity. Tax systems in different countries take various approaches to the problem of income taxation of partnerships. Some countries recognize partnerships as individual entities (*separate entity theory*), and sometimes even employ the same taxation rules as apply to companies.[1] In other countries, however, it is established that a partnership should be treated as an association of individual entrepreneurs *(aggregate theory)*. Consequently, income arising from involvement in a partnership is typically taxed at the level of its partners (natural or legal persons).[2] In the latter case, partnerships are transparent under applicable tax acts.[3] Within some legal systems, despite the fact that income generated by partnerships is subject to one-time taxation, partnerships are nevertheless obliged to report the level of generated income to relevant taxation bodies.[4]

The first of the solutions enumerated above is beneficial in that the choice of a partnership/company form is determined largely by attributes granted to such entities under the private law rather than the taxation method. The second of the solutions takes into greater account the nature of partnerships as a form of cooperation between partners (mainly natural persons) aimed at expanding the potential for their economic activity and creating a possibility for the division of costs and risks in the event of business failure. The recognition that partnerships are transparent entities results in the taxation of income at the level of partners. Consequently, legislators are required to take into account the specific nature of business operations conducted in partnerships when determining revenues and costs. With some exceptions, the Polish legislation has based the taxation of income on the second of the solutions discussed above, which relies on the premise that partnerships represent associations of partners. The approach is consistent with the legal status of civil law partnership, whereas commercial partnerships have been endowed with legal capacity in the domain of private law, which is why they exist as separate entities. The diverging approach existing within the framework of private and tax law leads to difficulties in determining the tax effects of economic events in commercial partnerships. The basic research method adopted in the study is the method of dogmatic analysis. The economic method of legal analysis was granted a supplementary role

2 General rules of taxation applicable to income generated from partnerships

Polish partnerships (with the exception of limited joint-stock partnerships) are not *de iure* income tax payers, neither with respect to personal income tax nor to corporate income tax. The tax acts in force essentially fail to include any provisions which are directly applicable to partnerships (since partnerships themselves are not subject to income taxes). Instead, the provisions defining rules of income taxation focus on partners. The objective and subjective scope of taxation is defined in Article 1 of the Act on Personal Income Tax. In conformity with the provision, the Act stipulates the rules and requirements for the payment of income tax by natural persons. The subjective scope of the Act on Corporate Income Tax, which is defined in Article 1 section 1, encompasses legal persons and companies in the process of incorporation. Pursuant to Article 1 section 2 of the Act on Corporate Income Tax (ACIT), the provisions of the Act also apply to organizational entities without a legal personality, with the exception of companies not having a legal personality, subject to provisions laid down in sections 1 and 3. Article 1 section 3 stipulates that ACIT has application to:

1) limited joint-stock partnerships having a registered office or management in the territory of the Republic of Poland;
2) companies without a legal personality which have their registered office or management in a another state in which, under the tax law regulations of that state, they are treated as legal persons and are subject in such state to taxation on the entirety of their income irrespective of the place where it is earned.

As the above regulations demonstrate, the Polish tax law incorporates both the concept of "multiple entrepreneurs" (with respect to the taxation of income generated by Polish partnerships) and the competing concept of "unity of enterprise" with regard to the taxation of foreign partnerships in cases where, based on the tax regulations of the state in which they have their registered office, they are treated as legal persons and are taxed on the entirety of their income), and (since 1 January 2014) also limited joint-stock companies.[5] The recognition of a foreign partnership as a corporate income taxpayer is determined by the tax regulations which are in force in the state in which the entity concerned has its registered office. The norms stipulated in the private law of a foreign state, particularly the question of having or not having a legal personality, however, are irrelevant for determining the scope of applicability of the Act.[6] The concept of corporate income taxpayer refers to commercial partnerships and civil law partnerships having a tax residence in a state in which such partnerships are not transparent in tax term (e.g. in Spain and Portugal). Partnerships which have their residence in such states are equated for tax purposes with companies.

In the light of the regulations discussed above defining the subjective scope of the acts on income taxes, it can be assumed that Polish partnerships (except for limited joint-stock companies) are tax-transparent entities, meaning that income generated from partnership activity is taxed at the partner level. The Supreme Administrative Court, in its judgement of 27 June

[1]In Portugal, for example, partnerships have legal personality and are subject to income tax also at the partnership level. Even civil law partnerships, which are not legal persons, are subjec to income tax. See M. Bandzmer *Status spółek osobowych w międzynarodowym prawie podatkowym [Status of partnerships in the international tax law]*, Warsaw 2015.

[2]W. S. McKee, W. F. Nelson, R. L. Whitmire, *Federal taxation of partnerships and partners*, Warren, Gorham & Lamont 1996, p. 8; A. D. Youngwood, D. B. Weiss, *Partners and Partnership—Aggregate vs. Entity Outside of Subchapter K.*, Tax Lawyer. Fall 1994, Vol. 48 issue 1, p. 39. 31; Ch. Trump, M. Graham, *In search of a Normative Theory of Partnership Taxation for International Tax (or How We Learned to Stop Worrying and Love Subchapter K)*, Taxes the Tax Magazine 2015, p.123.

[3]B. T. Borden, *Aggregate-plus theory of partnership taxation*, Georgia Law Review 2009, vol. 43, pp. 716-784; A. Monroe, *Integrity in Taxation: Rethinking Partnership Tax*, Alabama Law Review 2012, vol. 64, pp. 289- 334. N. B. Cunningham, L. E. Cunningham, *The Logic of Subchapter K: A Conceptual Guide to the Taxation of Partnerships*, St. Paul, West, 2011.

[4]For example in Australia, Singapore, South Africa or Sweden. See A. Easson, V. Thuronyi, Tax Law Design and Drafting, vol. 2; International Monetary Fund 1998, p. 9.

[5]Ł. Franczak, *Wpływ prawa podatkowego na popularność i zastosowanie instytucji spółki komandytowo–akcyjnej w Polsce [Effect of Tax Law on the Popularity and Application of the Institution of Limited Joint-Stock Company in Poland]*, Transformacje Prawa Prywatnego [Private Law Transformations] 2009, issue 3-4, p. 8.

[6]M. Bandzmer, *Kwalifikacja podatkowoprawna korporacyjnych podmiotów zagranicznych [Fiscal Law Qualification of Foreign Corporate Entities*], Monitor Podatkowy [Tax Monitor] 2013, issue 9.

2012,[7] emphasizes that the premise that income earned from involvement in a partnership which is not a legal person is taxed separately for each partner in proportion to the partner's share should not be taken to mean that every partner individually earns revenues and incurs costs related to the partnership's economic activity. In order to establish a partner's income from a partnership, it is necessary to determine the partnership's revenues and costs. Until the end of 2000, Article 8 of the Act on Personal Income Tax (APIT) indicated that income earned from involvement in a partnership without a legal personality was taxed separately for each person in proportion to their share. What the provision meant was that partnerships were not income taxpayers. Instead, the taxpayer status was held by partners, based on their income generated from partnership involvement. Consequently, a dual phase procedure had to be employed for income determination. The first phase involved determining a partner's income, and the second phase – the partner's income earned from partnership involvement. Starting in 2001, the above rules were amended by introducing the requirement to assign appropriate proportions of revenues and costs. Consequently, revenues, costs and expenditures not constituting costs are now determined at the partnership level, and the level of income is assessed at the partner level.[8]

The fundamental role in the taxation of income achieved from partnerships is played by tax rules set out in Article 8 section 1 of APIT and Article 5 of ACIT. The provisions of Article 8 section 1 of APIT and Article 5 section 1 of ACIT establish that the level of income attributable to a partner due to their partnership involvement is determined in proportion to that partner's right to participate in the partnership's profits. The same rule should be adopted for the determination of costs of generating revenue from the shared source which are attributable to a given partner. In accordance with Article 8 section 2 point 1 of APIT, the rule set out in Article 8 section 1 of APIT must be applied, as appropriate, for the settlement of costs of generating revenues. The rule laid down in Article 8 section 1 of APIT imposes an unambiguous obligation to determine the revenue of a partner in a partnership without a legal personality in proportion to that partner's right to participate in profits. Without evidence to the contrary, it is thus assumed that the rights to share in profits are equal. The provision stipulates that revenues earned in a partnership should be combined with other revenues, the income of which is subject to tax according to the tax scale set out in Article 27 section 1 of APIT. The proper application of rules contained in Article 8 section 1 of APIT for the settlement of costs of generating revenue requires adopting a proportion corresponding to a partner's share in their partnership's profits for:

a) calculating the share in the partnership's costs and for combining the costs with other costs incurred by the taxpayer to earn revenues, the income of which is taxable according to the tax scale in force;[9]
b) tax reliefs applicable to economic activity conducted in the form of a partnership not having a legal personality.[10]

According to Article 5 section 2 of ACIT, the rules set out in Article 5 section 1 must be applied, as appropriate, for the settlement of:

a) costs of generating revenues,[11]
b) expenditures not classifiable as costs of generating revenues,
c) tax exemptions and reliefs and income reduction,
d) taxation or tax base.

In order to assess the taxpayer's revenues, the following are necessary:[12]

a) determining the share in the partnership's profit in accordance with the partnership agreement or principles laid down in the Code of Commercial Companies and Partnerships;
b) determining an appropriate share in revenues attributable to the partner (taxpayer).

The revenues of partners being natural persons earned from their shares in a partnership, determined pursuant to Article 8 section 1 of APIT in accordance with Article 5b section 2 of APIT are recognized as revenues earned from the source mentioned in Article 10 section 1 point 3 of APIT, i.e. revenues from non-agricultural economic activity. Economic activity or non-agricultural economic activity, pursuant to Article 5a point 6 of APIT, refers to profit-gaining activity in the business of:

a) production, construction, trade and services,
b) prospecting for, exploration and extraction of minerals,
c) using products and intangible assets,

conducted in one's own name regardless of its outcome in an organized and continuous manner, generating revenues which are not classified as other revenues from sources enumerated in Article 10 section 1 points 1, 2 and 4-9 of APIT.

Tax authorities and administrative courts recognize that the general principle applicable to the qualification of revenues generated in partnerships is restricted through the operation of specific regulations. As justification, they point to the final part of the definition of non-agricultural economic activity which provides that "generated revenues are not classified as other revenues from sources enumerated in Article 10 section 1 points 1, 2 and 4-9 of APIT.[13] The Supreme Administrative Court, in its judgement of 6 March 2013[14] , ruled that a partner's revenues generated from involvement in a partnership not having a legal personality and conducting non-agricultural economic activity are recognized, pursuant to Article 5b section 2 of APIT, as revenues from non-agricultural economic activity on the stipulation that they may not be classified as revenues from sources enumerated in Article 10 section 1 points 1, 2 and 4-9 of the Act on Personal Income Tax. In the justification of the resolution of 26 April 2010[15], the Supreme Administrative Court stated that a situation in which management services within non-agricultural economic activity are provided by a partnership not having a legal personality is not subject to Article 5b section 2 of APIT, since revenues earned in relation with the provision of management services represent revenues achieved within non-agricultural economic activity in which the sole revenue source is the activity conducted personally.[16]

Whenever economic activity is conducted by a partnership which is not a legal person, revenues earned by a partner (payer of corporate income tax) from involvement in such a partnership, determined under Article 5 section 1 of ACIT, are recognized as revenues from economic activity (Article 5 section 3 of ACIT). Rules applicable to the taxation of taxpayers, i.e. partners in partnerships which are corporate income taxpayers and personal income taxpayers, are not identical. The disparity stems mainly

[7]File ref. no. II FSK 2439/10.
[8]H. Litwińczuk, *Opodatkowanie wspólników spółek nie mających osobowości prawnej [Taxation of Partners in Partnerships without Legal Personality]*, Przegląd Podatkowy [Tax Review] 2001, issue 7, p. 3.
[9]Taxpayers and small taxpayers starting economic activity may, in cases indicated in Article 22k section 7 of APIT, make one-off depreciation write-offs to an amount not exceeding EUR 50,000. For partnerships not being legal persons, the amount of depreciation write-offs refers to the total value of write-offs allocable (under Article 8 of APIT) to the partnership's partners.
[10]Judgement of the Supreme Administrative Court of 12 March 2013, file ref. no. II FSK 1421/11.
[11]Judgement of the Supreme Administrative Court of 30 June 2015, file ref. no. II FSK 1182/13: if a limited partnership suffers losses, the taxable base of its partner (being a legal person) is decreased (in proportion) or its "total" loss, which a company may settle within five years, is increased (Article 7 section 5 of ACIT).
[12]K. Gil, A. Obońska, A. Wacławczyk, A. Walter (eds.), *Podatek dochodowy od osób prawnych. Komentarz [Corporate Income Tax. A Commentary]*, Warsaw 2016, p. 89.
[13]Compare J. Marciniuk (ed.) *Podatek dochodowy od osób fizycznych. Komentarz [Personal Income Tax. A Commentary]*, Warsaw 2016, pp. 80-81. A partnership's acquisition of shares in a company in return for a contribution in kind in a form other than an enterprise, the disposal of securities by a partnership and – until the end of 2014 – the achievement of interest on bank deposits, consistently favour the classification of revenues of this type as revenues from capital gains or property rights.
[14]File ref. no. II FSK 1364/11.
[15]File ref. no. II FPS 10/09.
[16]A. Pęczyk-Tofel, M. S. Tofel, *Opodatkowanie dochodów ze „spółki menedżerskiej" (interpretacje podatkowe) [Taxation of income generated by "management partnerships" (tax interpretations)]*, Monitor Podatkowy [Tax Monitor] 2007, issue 5.

from differences in the construction of taxes with respect to revenue sources. The Act on Corporate Income Tax fails to provide a catalogue listing sources of revenue. Furthermore, it lacks regulations corresponding in terms of content to Article 5b section 2 of APIT[17] The Minister of Finance, in the general interpretation issued on 11 May 2012[18], pointed out that in Article 5b section 2 of APIT the legislation in place provides directly that whenever non-agricultural economic activity is conducted by a partnership not having a legal personality, revenues earned from partnership involvement by a partner being a natural person are regarded as revenues from economic activity. The clarification of the nature of income earned by a partner in a partnership which is included in the Act on Personal Income Tax – and the lack of a corresponding provision in the Act on Corporate Income Tax – stem from the fact that the former Act differentiates the method of taxation applicable to payers of that tax depending on the source of income (economic activity, property rights, capitals, economic activity conducted personally, etc.). No such differentiation is made in the provisions of the Act on Corporate Income Tax. With the exception of income from a share in profits of legal persons and income from agricultural activity, the Act in question employs a uniform qualification of income achieved by payers of the tax (i.e. without any division into income sources), and applies uniform rules for their taxation, treating them in principle as revenues relating to the conducted economic activity. Therefore, based on the opinion of the Ministry of Finance, it is to be assumed that a provision equivalent to Article 5b section 2 of APIT is not needed in the Act on Corporate Income Tax (…). This is because it is untenable to assume that any reasonable legislator would allow a possibility that the tax qualification of any given gain – identical as to its nature – would depend solely on whether the gaining entity is a natural or legal person. The rule of the legislator's rationality implies that any effects resulting from the interpretation of Article 5b section 2 of APIT which contradict the rule should be rejected, and those which are in accord should be adopted. Revenue (income) arising from being a partner in a partnership may not be recognized as revenues from capital gains. Consequently, amounts paid to a partner (legal person) do not constitute, for tax purposes, capital gain payments, and so the partnership is under no obligation to collect advances on income tax (from any title or source) from amounts paid to (placed at the disposal of) the partner.[19] For the avoidance of doubt, the Act of 8 November 2013[20] which came into effect on 1 January 2014 was provided with Article 5 section 3 of ACIT stipulating that in situations where economic activity is conducted by a company not being a legal person, revenues earned by a partner from involvement in such a partnership are to be recognized as revenues from economic activity.

The concept of determining income at the partner level, on the basis of share in the partnership, has created a possibility to individualize tax settlements for the partners.[21] Since partnerships may involve natural and legal persons, the taxation of partnership profits is regulated by norms of specific substantive law laid down in two separate tax acts.[22]

The legislation relies on the principle of accrual-based identification of revenues and costs generated through partnerships by their partners.[23] The rule of assigning partnership revenues and costs to partners applies regardless of whether partners during the period in which they keep a share in the partnership actually receive any payments or no payments are made (e.g. the partnership retains profits for further investment). The assumption that revenues generated by a partnership are taxed at the level of its partners irrespective of any payments received from the partnership concerned (i.e. regardless of whether partners have obtained an actual financial gain) means that cash flows taking place between the partnership and its partners should be neutral in tax terms. If the revenues and costs related to partnership involvement were taxed "on an ongoing basis" (i.e. on the accrual basis) and were then taxed again – in the case of actual cash flows between the partnership and its partners – on the cash basis, there is a risk of double taxation. Consequently, deviations from the accrual principle may be introduced only exceptionally, if the legislator includes an explicit provision to that effect in the tax act.

Pursuant to Article 24 section 1 of APIT, in the case of taxpayers keeping books of account, income from economic activity is deemed to refer to income reported in correctly kept books reduced by the amount of tax-free income and increased by expenditures not classifiable as costs of generating revenues previously charged against costs of generating revenues. The income of taxpayers achieving income from economic activity and keeping books of revenues and expenditures is determined in line with the principles laid down in Article 24 section 1 of APIT. The obligations contained in the Accounting Act are binding only upon natural persons, civil law partnerships of natural persons, registered partnerships of natural persons and limited liability partnerships, if their net revenues from the sale of commodities, products and financial operations for the preceding financial year constitute at least the Polish zloty equivalent of EUR 1,200,000 (Article 2 section 1 point 2 of the Accounting Act). If partners to a civil law partnership or a commercial partnership include at least one entity that is not a natural person, the partnership is obligated to follow the provisions of the Accounting Act.

The regulation contained in the Code of Commercial Companies and Partnerships which permits partners to freely define the obligation to participate in the partnership's costs, independently of rules adopted for the settlement of profit, refers to settlements between partners, and hence relations under civil law, without affecting tax law effects regulated by norms laid down in the tax law[24]. In this regard, the tax law introduces provisions differing from the Code of Commercial Companies and Partnerships. Under Article 51 of the Code of Commercial Companies and Partnerships, every partner is entitled to an equal share in profits and participates in losses in the same proportion irrespectively of the type and value of the contribution. The provision is dispositive in nature (which stems from the provisions of Article 37 § 1 of the Code of Commercial Companies and Partnerships). What this means is that partners are free to differently define in the partnership agreement the method applicable to the division of profit and to the determination of costs associated with partnership activity which are assigned to individual partners. Solutions adopted in the partnership agreement and in partners' resolutions, providing for disproportionate shares to be had by different partners in the partnership's revenues (compared to their participation in costs), do not translate into tax obligations in a straightforward manner. Provisions laid down in the Code of Commercial Companies and Partnerships should not be viewed as a source of a tax obligation and taxation rules other than those contained in relevant tax acts.[25] Partners to partnerships are free to define the right to share in the partnership's profit at any proportion (permitted under the Code of Commercial Companies and Partnerships) that will be employed for the settlement of revenues arising from the share in the partnership. Nevertheless, the same proportion should be consistently applied for settling costs of generating revenues for tax purposes.[26] The position

[17]Judgement of the Supreme Administrative Court of 20 April 2015, file ref. no. II FSK 2459/13.
[18]File ref. no. DD5/033/1/12/KSM/ DD-125, Official Journal of the Minister of Finance, 18 May 2012, item 24.
[19]Individual interpretation issued by the Director of the Inland Revenue Chamber in Katowice on 2 February 2016, file ref. no. IBPB-1-1/4510-217/15/BK.
[20]Polish Journal of Laws 2013, item 1387.
[21]A. Lewicki, *Opodatkowanie zysku spółki osobowej – wybrane problemy [Taxation of profit in partnerships: selected problems]*, Glosa 2001, issue 6, p. 3.
[22] G. Matysek, *Opodatkowanie dochodów spółek osobowych – konieczność zmian [Taxation of partnership income: need for changes*], Prace Naukowe Uniwersytetu Ekonomicznego we Wrocławiu [Research Papers of Wrocław University of Economics] 2013, issue 306, p. 249.
[23]Judgement of the Supreme Administrative Court of 22 May 2014, file ref. no. II FSK 1471/12.
[24]Judgement of the Supreme Administrative Court of 6 October 2011, file ref. no. II FSK 704/10.
[25]Judgement of the Supreme Administrative Court of 30 June 2015, file ref. no. II FSK 1182/13.
[26]Judgement of the Voivodship Administrative Court in Warsaw of 11 February 2011, file ref. no. III SA/WA 1380; Individual interpretation of the Director of Inland

excluding the possibility of applying different proportions for the settlement of revenues from involvement in a partnership not being a legal person, and for the settlement of costs of generating revenues, has been consistently rejected by administrative courts.[27] In the judgement of 1 June 2011 [28] , the Supreme Administrative Court rules that if a tax act stipulates specific tax law effects with respect to rules of determining revenues and costs of generating revenues for partnerships to a registered partnership, the taxpayer has no grounds to demand a revocation or modification of any such effects on the sole claim that the partnership agreement concluded by the partner provides otherwise. In fact, the opposite correlation is in place: the partnership agreement should take into account legal norms of an absolutely binding nature which are laid down in the tax law, also with respect to rules governing the assignment of revenues and costs to partners, and to settlement periods during which appropriate values should be assigned. In the judgement of 30 June 2015, the Supreme Administrative Court ruled[29] that the reference, contained in Article 8 section 2 point 1 of APIT, to an appropriate application of principles set out in Article 8 section 1 of APIT (for the settlement of costs of generating revenues, expenditures not classifiable as costs of generating revenues and losses) does not modify the provision adopted in section 1 introducing a rule for the settlement of revenues in such a manner as to allow a method of determining partner shares in costs of generating revenues or from involvement in a partnership not being a legal person other than in proportion to the partners' right to participate in profits.

When concluding a partnership agreement, partners are free to establish that their share in the partnership's profits and losses will be agreed on a monthly basis, depending on the actual work contribution made by each of the partners or the revenue generated by respective partners for the partnership in any given month. Consequently, the share in profits and losses attributed to respective partners may change up to twelve times over the space of one year. Both the provisions of the Civil Code (in Article 867) and the Code of Commercial Companies and Partnerships (in Articles 48 and 51) describing the principles governing partners' due share in profits and losses do not exclude the possibility that the assignment changes on a month-to-month basis in accordance with the terms of the partnership agreement. Therefore, there is no obstacle in the current laws (including the tax law) that would preclude providing the partnership agreement with a clause stating that the share of respective partners in the partnership's profits and losses is to be determined in proportion to the revenue they generate for the partnership or the amount of work they put in. In the opinion of tax authorities, the Act on Personal Income Tax does not ban the adoption of partnership agreements which specify the share of partners in profits and losses differently depending on the month, as laid down in applicable provisions of the partnership agreement[30]. It is also an acceptable practice to amend partnership agreements with respect to provisions defining a partner's share in profits.[31] Such amendments become effective the moment they are implemented, unless partners agree on a different effective date for amendments in the future. It is crucial, though, that the principles governing partners' share in profits are defined in a manner allowing their unambiguous assignment to respective partners. In situations when a partner's right to share in profits cannot be unambiguously determined from the partnership agreement because of specific provisions that make the scope of that right variable in time and fluid, there is a risk of tax authorities assuming that the partners' rights to a share in profits are equal and, consequently, the revenues and costs of generating them should also be divided equally between the partners.[32] In the opinion of tax authorities, if the share in profit at the end of the tax year changes in relation to the share adopted for the purpose of calculating income tax advance payments, then the level of income for the tax year in question should be established on the basis of the share in profit determined at the end of the tax year rather than the share in profit adopted for the calculation of individual income tax advance payments.[33] The method for the assessment of share in the partnership's revenues/costs in such cases will crucially depend on the rules of participation in profit indicated in the partnership agreement.

Unlike in companies, the payment of profit in partnerships does not require partners to adopt a resolution on the allocation of profit for payment. This is the position taken by the Supreme Court in its judgement of 3 July 2008.[34] Also, it needs to be stressed that profit defined as an excess of the partnership's property over and above the value of partners' contributions is objective in nature. Another vital factor is that partners may receive an advance payment towards a future profit even if their partnership does not generate any profits. The above claim is consistent with rulings passed by the Supreme Court.[35] The most important provisions regulating advance payments towards profit must be included in the partnership agreement. At the same time, however, the decision-making powers with regard to payments made on an ongoing basis should be left to the partners. Yet another aspect must be mentioned. If during the financial year a partner has collected – through advance payments – a sum exceeding the portion of the annual profit attributable to that partner, there is no obligation to return the surplus. The approach is justified by the fact that, ultimately, partners are personally liable for the partnership's obligations. In the judgement of 5 March 2009, the Supreme Court ruled[36] that if a partnership fails to achieve a profit, the partner who (through the consent of all other partners) has collected advance payments towards participation in future profits, has no obligation to return any amounts to the partnership by way of settlement of the advance payments collected. This is because settlements are made in the consecutive financial year in which the partnership generates a profit. Under the tax law, any advance payments collected by a partner are treated as gratuitous benefits provided by the partnership to the partner (Article 11 section 2a of APIT, Article 12 section 1 point 2 of ACIT). In such cases, the partner's revenue is equal to the amount of interest which a partner would be required to pay when obtaining a loan equivalent to the difference between advance payments collected by a partner and the amount of profit due to that partner.[37]

The difficulty with determining the principles of taxation applicable to partnerships is also manifest in other constructs and

Revenue Chamber in Katowice issued on 4 August 2015, file ref. no. IBPB-1-1/4511-205/15/BK.

[27]Compare judgement of the Supreme Administrative Court of 1 June 2011, file ref. no. II FSK 140/10, or judgements by Voivodship Administrative Courts in Gdańsk: 26 November 2009, I SA/GD 731/09 and 10 December 2009, I SA/GD 729/09; and in Cracow: 2 March 2010, I SA/KR 1592/09.

[28]File ref. no. II FSK 140/10.

[29]File ref. no. II FSK 1267/13.

[30]Individual interpretation of 24 January 2014, file ref. no. IBPBI/1/415-1109/13/AB.

[31]Judgement of the Supreme Administrative Court of 11 June 2015, file ref. no. II FSK 1527/13: the term "due revenue" (Article 12 section 3 of ACIT) from the involvement of a legal person in a partnership should – for the purpose of calculating advance payments for corporate income tax – be interpreted as referring to a part of the revenue, assignable to a partner, generated in the partnership during its financial settlement period, which corresponds to proportions applicable to the share in profit existing on the date of arising of the obligation with respect to the advance payment (Article 5 section 1 of ACIT). A change in the proportions during the tax year, even if the changes are considered as being in force from the beginning of the year, produces specific effects for the future, meaning that the "new proportions" for sharing in the profit must be taken into account beginning from the month in which the partnership agreement was amended to introduce them. Determining the amount of the consecutive (i.e. calculated after the amendment of the partnership agreement) advance payment requires calculating the amount of income gained from the beginning of the year according to new rules and subtracting from that sum the amount of advance payments already paid for the preceding months.

[32]Judgement of Supreme Administrative Court of 6 October 2011, file ref. no. II FSK 704/10.

[33]Individual interpretation issued by the Director of the Inland Revenue Chamber in Katowice on 4 March 2015, file ref. no. IBPBI/1/415-1457/14/AB and individual interpretation issued by the Director of the Inland Revenue Chamber in Katowice on 12 January 2016, file ref. no. IBPB-1-1/4511-648/15/EN.

[34]File ref. no. IV CSK 101/08. In registered partnerships, as opposed to companies (Article 191 § 1 and Article 347 § 1 of the Code of Commercial Companies and Partnerships), profit payment is not conditional on the partners adopting a resolution on the allocation of profit for payment. Profit, defined as an excess of partnership's property over and above the value of partners' contributions is objective in nature. It arises and exists irrespective of whether the partners adopt a resolution approving the financial statement for the past financial year. In partnerships preparing financial statements profit results from a given partnership's balance sheet.

[35]Judgement of the Supreme Court of 5 March 2009, file ref. no. III CSK 290/08.

[36]File ref. no. IV CSK 101/08.

[37]Individual interpretation issued by the Director of the Inland Revenue Chamber in Katowice on 25 November 2014, file ref. no. IBPBI/2/423-1043/14/PC.

concepts present in the tax law and private law. In the light of Article 8 section 1 of APIT, there is a difference between profit earned by a partnership and the source of the profit (e.g. donation) and a partner's revenue from participating in a partnership's profit which is subject to personal income tax.[38]. Based on provisions laid down in Article 14 section 1 of APIT, revenue from economic activity refers to amounts due, either actually received or not, after the subtraction of the value of returned goods, granted rebates and discounts. In the case of taxpayers selling goods and services which are subject to the tax on goods and services, revenue from the sale should be thought of as referring to the total revenue reduced by a due amount of tax on goods and services. In principle, it encompasses all revenues generated from economic activity conducted by a partnership with the exception of revenues defined in Article 14 section 3 of APIT. As set out in Article 44 section 1 point 1 of APIT, taxpayers achieving income from economic activity referred to in Article 14 are obliged, without any request to that effect, to make income tax advance payments over the course of the tax year in conformity with rules provided in section 3, subject to sections 3f-3h. Accordingly, partners to a partnership are obligated to make requisite advance payments during the tax year. Payment arising from the division of profit is a reflection of income earned by partners from their economic activity conducted in the form of a partnership. That income, as indicated above, is taxed at the level of each partner in proportion to the right of respective partners to share in the profits which is specified in the partnership agreement. In view of the above, the payment of share in the annual balance-sheet profit of a partnership made pursuant to Article 52 § 1 of the Code of Commercial Companies and Partnerships, will represent a tax neutral activity for the partnership's partners, since profit achieved in the partnership represents, in point of fact, the already taxed gains of its partners.[39]. The profit obtained by division may not correspond in terms of actual amounts to the income reported by a partner during the tax year. However, it must be noted that tax regulations are concerned with the right to a share in profit rather than to claims for payment (according to the agreed proportions at the end of the financial year) or the amount actually received for partnership involvement. In effect, tax applies to the amount of difference between revenues and costs determined for taxation purposes, not amounts actually received by partners[40].

Until the amendment of the income tax acts which came into effect on 1 January 2015, it was debatable whether the payment of a part of the profit due to a partner on an in-kind basis is taxable. The positions taken by administrative courts and tax authorities were divergent. While it is true that the majority of courts ruled that the transfer of ownership (e.g. of property) via profit payment did not constitute revenue-generating disposal (not being a transaction performed for consideration),[41] a major part of tax authorities classified the transfer of non-cash (in-kind) benefits as disposal against consideration[42]. In the opinion of courts, "since it does not stem directly from the provisions of law that the payment of a non-cash dividend causes the arising of a tax obligation for the taxpayer, then *a contrario* the catalogue of revenue sources may not be *a priori* extended for income tax purposes".[43]

The doubts were removed by the introduction of Article 14 section 2e of APIT and Article 14a of ACIT, under which if a taxpayer – through the performance of a non-cash benefit – settles either in its entirety or in part – an obligation (…), the taxpayer's revenue is equal to the amount of obligation settled as a consequence of the benefit. However, if the market value of the non-cash benefit in question is higher than the amount of obligation settled through the benefit, the revenue is determined as being equivalent to the market value of the non-cash benefit concerned. The provision set out in Article 19 of APIT (Article 14 sections 1-3 of ACIT, as appropriate) is applied accordingly. Under Article 14 section 2f and Article 14 a section 2, the principles are applicable, as appropriate, to cases involving the performance of a non-cash benefit by a partnership not being a legal person. Consequently, the payment is equated with disposal against consideration of a thing or property rights, and is therefore subject to taxation. The payment of non-cash profit to a partner represents revenues for partners to a partnership in proportion to their share in profits. Another vital aspect is the problem of accurate valuation of assets transferred to a partner. Preferably, their value should correspond to the value of profit paid.

With regard to capital share in the partnership, every partner is entitled to receive annual interest equal to 5% of the value of the capital, even if the partnership has recorded a loss. The interest is calculated based on the value of the partner's capital share which is equal to the value of the contribution made by that partner. Article 53 of the Code of Commercial Companies and Partnerships, which provides the legal basis for the payment of interest, is dispositive in nature. What this means is that partners are free to exclude the application of the provision or modify it in the partnership agreement. Interest paid in respect of that represents, in the opinion of tax authorities[44], revenue from the so-called "other sources" which are mentioned in Article 10 section 1 item 9 of APIT. The payment of interest on capital share is independent of income generated from economic activity, hence revenues achieved in this manner are not classified as revenues from economic activity. Likewise, revenue arising from the payment of interest on capital share may not be classified as a source of revenue in the form of monetary capital, for Article 17 section 1 of APIT does not mention interest paid on the value of capital share in a partnership as revenue from that source and – a point to be made – the catalogue contained in that provision is exhaustive in nature. Revenues can be classified as coming from other sources in situations where a specific revenue cannot be classified into sources of revenue mentioned in Article 10 section 1 points 1-8 of APIT. Consequently, revenues from other sources include those revenues which do not arise from sources discussed above and, at the same time, constitute income within the meaning of the Act on Personal Income Tax. The classification means that revenue from interest paid on the capital share is taxed according to the tax scale in force, without an option of choosing the flat rate, and may not be settled together with revenues and costs associated with economic activity. Revenue arising from interest paid pursuant to Article 53 of the Code of Commercial Companies and Partnerships cannot be reduced by the amount of loss in economic activity.

Revenues from activity performed within the framework of a partnership by a natural person can be taxed under general principles. In this case, tax is calculated according to the applicable tax scale after subtracting costs of generating revenue. Revenues from activity performed within the framework of a partnership by a natural person can be taxed with a linear tax rate. In such cases, the tax rate of 19% is applied after subtracting costs of generating revenue.

3 Conclusion

For persons choosing a legal form of conducted business activity the manner of company taxation is one of the main selection criteria. Partnerships are different from joint-stock companies mainly because of the lack of legal personality and the

[38]Judgement of the Supreme Administrative Court of 8 January 2013, file ref. no. II FSK 1347/11.
[39]Compare the individual interpretation issued by the Director of the Inland Revenue Office in Warsaw on 17 April 2014, file ref. no. IPPB1/415-131/14-2/EC.
[40]A. Pęczyk, M. S. Tofel, *Podatkowe skutki zmiany wysokości udziału w zysku spółki osobowej w roku podatkowym [Basic effects of changes in the share of partnership profit during the tax year]*, Prawo i Podatki [Law and Taxes] 2006, issue 11, p. 13.
[41]Judgement of the Voivodship Administrative Court of 30 December 2013, file ref. no. I SA/Ke 658/13; judgement of the Voivodship Administrative Court of 18 February 2014, file ref. no. I SA/Wr 2375/13; judgement of the Supreme Administrative Court of 8 February 2012, file ref. no. II FSK 1384/10.
[42]Individual interpretation issued on 20 February 2013, no. IBPBI/2/423-1538/12/MS; individual interpretation issued on 30 September 2011, file ref. no. IBPBI/2/423-787/11/JD.
[43]Judgement of the Voivodship Administrative Court of 5 December 2012, file ref. no. I SA/Po 699/12.
[44]Individual interpretation issued on 16 March 2010, file ref. no. ITPB1/415-997a/09/TK.

possibility of personal liability for company liabilities. The most important differences are visible in income taxes, since partnerships are not granted the taxpayer status, which makes them tax transparent entities. Polish legislator has assumed that income in partnerships is taxed with income tax only at the level of the partners (only the partner is the taxpayer, not the partnership). The adoption of separate principles of taxation of partnerships should result from the specific structure of these companies, which is different from the structure adopted by the legislator in the case of joint-stock companies. The most important structural difference between them is due to the fact that partnerships are the unity of persons, and not the unity of capitals, as is the case of joint stock companies.

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