

THE UNIVERSITY OF WARSAW

# Taxation of non-profit organizations

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Poland

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## The list of abbreviations

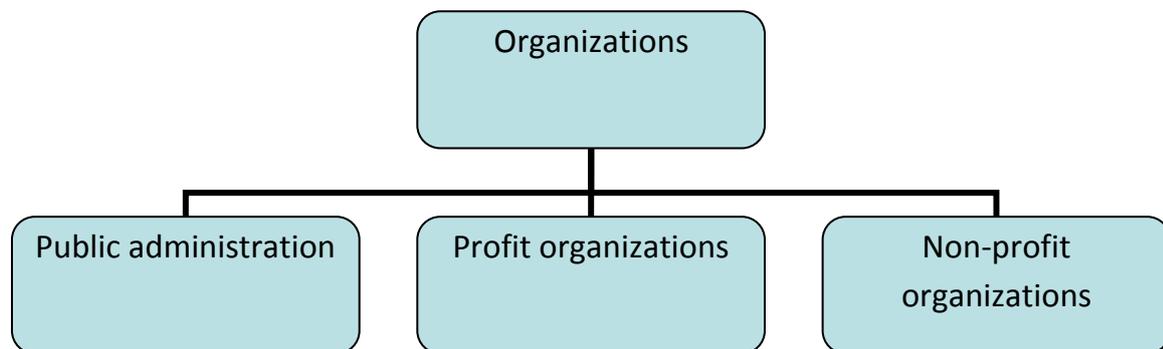
The Constitution	The Constitution of Republic of Poland from 2 <sup>nd</sup> August 1997 (Dz.U. 1997 Nr 78 Poz.483)
The Council Directive 2004/106/EC	The Council Directive 2004/106/EC from 16 <sup>th</sup> November 2004 (Dz.U. L 359 , 04/12/2004 P. 0030 – 0031)
The CIT Act	The Corporate Income Tax Act from 15 <sup>th</sup> January 1992 (Dz.U Nr 21, poz. 86)
The PIT Act	The Personal Income Tax Act from 26 <sup>th</sup> July 1991 (Dz.U 2010 Nr 51, poz. 307)
The Public Benefit Act	The Act on public benefit activity and on volunteer work from 24 <sup>th</sup> April 2003 (Dz.U. 2010 Nr 234 poz. 1536)
The Company Law Act	The Company Law Act from 15 <sup>th</sup> September 2000 (Dz.U. 2000 Nr 94, poz. 1037)
The Law on associations	The Law on associations from 7 <sup>th</sup> August 1989 (Dz. U. 2001 r. Nr 79 poz. 855)
The Act on foundations	The Corporate Income Tax Act from 6 <sup>th</sup> August 1984 (Dz. U. 1991 r. Nr 46 poz. 203)
The VAT Directive	The Council Directive 2006/112/EC of 28 <sup>th</sup> November 2006 on the common system of value added tax (Dz.UrzUEL.2006.347.1)
The VAT Act	The Act on value added tax from 11 <sup>th</sup> March 2004 (Dz. U. 2011 r. Nr 177 poz. 1054)
The VAT Ordinance	The Ordinance of Finance Minister from 4 <sup>th</sup> August 2011 on execution of certain provisions of the act on the

	value added tax (Dz.U. 2011 Nr 73, poz.392)
The Inheritance and gifts tax Act	The Inheritance and gifts tax Act from 28 July 1983 (Dz.U. 2009 Nr 93, poz. 768)
The Law on taxes and local levies	The Law on taxes and local levies from 12 January 1991 (Dz.U. 2010 Nr 95, poz. 613)
The Law on civil acts tax	The Law on civil acts tax from 9 <sup>th</sup> September 2000 (Dz.U. 2010 Nr 101, poz. 649)
The Law on stamp tax	The law on stamp tax from 16 <sup>th</sup> November 2006 (Dz.U.2006 nr 225 poz.1635)

## Introduction

Traditionally non-profit organizations are called the third sector<sup>1</sup>. This name reflects the concept of division of social-economic activities on three sectors. The first one is public administration, the second are profit organizations (business, private sector), whereas the third one: organization which aim is not connected with the profit. The division is presented on the chart.

Picture 1: The classification of organizations.



The source: the own study.

There are different terms used for non-profit organizations. They are called: charitable organizations, voluntary sector or independent sector.

The third sector is defined by the set of features. The most popular definition is the one formulated by John Hopkins. It includes several the most significant features. The first feature refers to the existence of the structure of organizations and its formal registration. On the base of the second one it is assumed that the organizations is independent from public authorities. It should be also non-profit. It means that the aim of activity cannot be to gain profits. What is more, the organization has to be sovereign and self-governing. There cannot be any compulsion in joining organization. It is said that when all listed requirements are fulfilled, non-profit organization exists.

The third sector may be understood in two different ways: the broader and narrow sense. The broader scope of the term includes very diversified

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<sup>1</sup>online: [www.ngo.pl].

types of organizations, whereas non-profit organizations in the narrow sense range mainly to foundation and different types of associations.

The non-profit organizations has to be distinguished from social organization. The social organization is a term which relates to broader scope of organizations than only non-profit one, e.g. a trade union is a social organization but not non-profit one.

In Poland contemporary position of non-profit sector has been strongly influenced by communistic past. The similar situation may be noticed in the whole Central and Eastern Europe where civic society has rather short history. This results mainly in lower interest of Polish citizens in any kind of non-profit activity. According to some researches<sup>2</sup>, only a quarter of Polish citizens are members of an non-profit organization, whereas in Western Europe more than the half of citizens participate in. As it is assessed the crucial reason for the sluggish growth are poor economic resources. The non-profit organizations are not subsidized by government. In order to maintain, they very often have to run business. Nevertheless, the existence of non-profit sector cannot be undervalued. It is still the sector which is going to develop and become stronger and stronger. The non-profit organizations in Poland cooperate with well-educated personnel. 60% of non-profit workers possess higher education which stands for three times more than in the whole economy<sup>3</sup>. Only between 2002 and 2004 there has been noticed the growth of number of non-profit organizations of 26%. Taking into consideration the worldwide data, the role of non-profit organizations seems to be significant. The non-profit sector revenues in 35 examined countries of 1,3 bln dollars annually. In this way it stands for the seventh economy in the world<sup>4</sup>.

Bearing in mind all the data, it is worth examining the legal framework of non-profit activity in Poland. As it was noticed, the sector is still growing, therefore its examination is even more vital. The main aim of this study is, however, the taxation of the non-profit organization in Poland. There are several questions which the author of this study is concentrated on. The

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<sup>2</sup> Sektor non-profit w Polsce. Wybrane wyniki badań statystycznych zrealizowanych przez GUS na formularzach SOF, Warszawa 2009, dostęp online: [[http://www.stat.gov.pl/gus/5840\\_5913\\_PLK\\_HTML.htm](http://www.stat.gov.pl/gus/5840_5913_PLK_HTML.htm)].

<sup>3</sup> Gumkowska M., Herbst J.: Podstawowe fakty o organizacjach pozarządowych – raport z badania 2004. Stowarzyszenie Klon/ Jawor, Warszawa, 2005, s. 20; za: Witek-Crabb, A. (2006). Specyfika zarządzania strategicznego w organizacjach non-profit. Organizacje komercyjne i niekomercyjne wobec wzmożonej konkurencji oraz wzrastających wymagań konsumentów, (red.) A. Nalepka, Wydawnictwo Wyższej Szkoły Biznesu – National-Louis University, Nowy Sącz, s. 129-138.

<sup>4</sup> Witek-Crabb, A., op. cit.

first takes into account the possible ways of undertaking non-profit activities. What legal forms are provided for in Polish legal acts and what general rules are applied to them is the theme of the part I of this study. In the part II the author analyses direct taxation of non-profit activities. In the context of direct taxation it has to be noticed that Polish income tax law differs two basic ways of taxation. The first one relates to the taxation of taxpayers who have legal personality. Their actions are regulated by the CIT Act. The second one provides for natural persons. Their tax situation is settled by the PIT Act. Taking into account the specific character of non-profit sector in Poland the relevant tax act in the study will be the CIT Act. The provisions which may be found in the PIT Act relates to non-profit activities (rather than organizations) undertaken by natural persons. However, they play significant role in the development of non-profit organizations. Therefore, they will be also presented herein.

In the III part there are analyzed basic issues regarding indirect taxation. The IV part refers to inheritance, estate and gift taxes which are also relevant to non-profit organizations. In the last part there are described other taxes and levies which cannot be omitted in this thesis. There are mainly discussed taxes on civil acts.

The detailed investigation of tax aspects of non-profit activity in Poland, especially legal rules which are of crucial meaning for their existence, is intended to assess the influence of legal framework on development of non-profit sector in Poland. In conclusions the author tries to summarize the findings of the study, draw essential conclusions and eventually set some suggestions *de lege ferenda*.

## 1. Legal framework

### 1.1. General remarks

Non-profit activity may be distinguished between an activity which is undertaken from time to time by any kind of entity (both natural persons and legal persons) and the one which is carried in the form of organization as a charity. The author is going to concentrate mainly on organized form of non-profit activities. Nevertheless, the first type of it will be mentioned as well when analyzing some tax aspects of non-profit activity.

The non-profit organizations may have huge impact on the shape of the society. In the development of the third sector the legal system plays a vital role. The right of founding associations and foundation has been guaranteed by the Constitution. Under art. 12 of the Constitution the Republic of Poland assures the freedom of establishing and functioning of trade unions, social and professional organizations of farmers, associations, civic movements, other voluntary unions and foundations. This provision is a foundation of any other legislation in the respect of non-profit organization.

Taking into account the special role of not for profit activity, the legislator provided for special tax rules for those organizations. All given rules are of a statutory character, although some of them were initially ideas born by the jurisprudence. Preferential provisions may be found both in the direct and indirect taxation. They are mainly based on tax exemption. In this way the legislator encourages to donate different socially vital values realized by non-profit organizations.

The scope of goals which are within not for profit activities is wide. It is the Public benefit act which defines that non-profit organizations perform activities which are treated as in public interest. The area of these activities includes catalogue of activities, e.g. work to support the development of local communities or science, education, coaching, and upbringing.<sup>5</sup>

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<sup>5</sup> Under the art. 4 of the Public benefit Act there are exemplified activities: Social assistance, including aid offered to disadvantaged families and individuals, and ensuring equal opportunities to such families and individuals, Professional and social integration and reintegration of persons threatened with social exclusion, charity work, preserving national traditions, sustaining Polish identity and developing national, civic, and cultural awareness, work to support national and ethnic minorities and regional languages, protection and promotion of health, work to support the disabled, promoting employment and professional activation of the unemployed and individuals threatened with job loss, promoting equal rights of women and men, work to support the elderly, promotion of economic growth and entrepreneurship, promotion of the development of new

The pointed provision is not a part of a Polish tax law. Nevertheless, it is worth mentioning because Polish tax acts very often refers to the Public benefit act. Tax law defines purposes which allow non-profit organization to benefit from tax exemption autonomously. They are discussed in the part 2 of this thesis. At this point of the thesis it is worth pointing that Polish tax law distinguishes two types of exempted entities. The first type is defined by the purpose stipulated in the tax law (the CIT Act). The second type is exempted thanks to the status of a public benefit organization (this entity has to realize one of mentioned values under art. 4 of the Public benefit act).

It has to be stressed that in Poland non-profit activity may be undertaken only in the form having legal personality. This conclusion is a result of analysis of civil law more than tax law. The provisions of tax law acts (mainly the CIT Act) do not require any special form of legal person for qualification as a non-profit entity. What is more, the CIT Act does not recognize the notion: a non-profit activity. If any preferential tax rules are provided, they are mainly combined with specific goals set forth in a statute. The only exception are public benefit organizations which will be commented herein. These organizations benefit from special tax status just on the basis of having the status of public benefit organizations. Therefore, special rules are provided for legal persons in the CIT Act. Preferential regime for natural persons refers only to deductions of gifts and contributions in the person of the donor or contributor (this is commented in the part II of the thesis).

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technologies, inventions and innovation transfer and implementation of new technologies for companies, work to support the development of local communities, science, education, coaching, and upbringing, recreation of children and youth, culture, art, and the protection of culture and national heritage; promoting physical culture and sports, ecology, animal protection, protection of natural heritage, tourism and knowledge touring, public order and security, national defence and the activity of armed forces of the republic of Poland, promoting and protection of human and civil rights and freedoms, work to support the development of democracy, rescue systems and protection of residents, aid to victims of calamities, natural disasters, armed conflicts and warfare in Poland and abroad, promoting and protecting consumer rights, work to support European integration, and the development of contacts and co-operation between societies, promoting and organising volunteerism, aid extended to Poles and Polish community abroad, work to support the veterans and persons who have undergone state repression, promotion of the republic of Poland abroad, work to support families, promote motherhood and parenthood and to promote and protect the rights of children, prevention of addictions and social pathology, work to support non-governmental organisations and entities listed in article 3, para 3 active in the areas listed in subpara 1-32.

This catalogue is open and the Council of Ministers may, in an ordinance, define tasks within a scope other than those specified above as activities in the public interest, in recognition of their particular public benefit.

## 1.2. Legal forms of non-profit activity

Taking into account that the legislator combined possibility of benefiting from special tax regime with specific goals which an entity has to have in its statute, only a few forms of legal entities may benefit from special tax rules. The issue of legal form which enables to undertake non-profit activity is provided for in special acts regulating particular entities. On the ground of Polish law a charity may exist in the legal form of a company, an association and a foundation. Pursuant to the article 151 of the Company Law Act both limited liability company and joint stock company may be established in any legally accepted purpose. This is why, it may be stated that both types of companies may carry non-profit activity. The prerequisite is that this special kind of activity should be pointed in their statute. Both companies have legal personality and their tax status is regulated by the CIT Act. They have to be registered by the Registry Court. In contrary to companies, no partnership may be recognized as a non-profit organization. Pursuant to relevant provisions of Company Law Act, all partnerships are established in order to run business. This phrase "to run business" is understood as they are formed for profit. Non-profit organizations may perform profit activity only as a supportive task.

Two another legal forms are associations and foundations. Both types of organizations have noncommercial purpose of their activity. It means that pursuant to the provisions of the Law on associations and The Act on foundations these organizations can be established on condition that they are non-profit. They both are also legal persons. Nevertheless, there is a possibility to form a kind of an association, which is called a simple association and does not have legal personality.

An association is a voluntary, self-governing and stable union which acts non-profit.<sup>6</sup> The right to form an association is an attribute of natural persons. The legal person may only have a status of a supporting member. Foreigners may associate but if they are living abroad, they are not allowed to form an association. The purpose of an organization is declared by members of an association. There is however general rule that an association is formed in order to fulfill needs of its members. An association is supervised by local authorities. If an association does not abide the law, a court may eventually dissolve an association. The

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<sup>6</sup> K. Majchrzyk, *Fundacja a stowarzyszenie – podobieństwa i różnice. Komentarz praktyczny*. Vademecum doradcy podatkowego.

provisions of the Law on association allow associations to participate in international organizations.

In contrary to an association, in the Act on foundation there are provided for possible goals of a foundation. It may be established only to "pursue socially or economically useful objectives that are consonant with the basic interests of the Republic of Poland; in particular, such objectives as health protection, advancement of the economy and of science, education, literacy, culture, art, social services, environmental protection and the protection of historical landmarks." A foundation may be formed by natural persons (both foreigners and citizens) as well as foreign or domestic legal persons. There is a prerequisite that it has to have its premises in Poland. What is more, it has to be formed in order to fulfill needs of persons who are not members of a foundation. A foundation does not have its members. The term of a foundation is understood as a fortune which is given by a founder.

All herein described legal forms: associations, foundations, companies (acting non-profit), but also church organizations may apply for the status of public benefit organizations. As was afore said, it is the only legal form which is recognized by Polish tax law and associated with public benefit activity. It is vital to underline that Polish tax law differs public benefit organizations and other organizations which may stand for the third sector (e.g. associations). There are provided for them different special tax rules. As a consequence, there are also different requirements which specific organizations has to fulfill in order to be granted tax benefits.

Public benefit organization does not form another type of legal entity. It is special legal status which any of hereinabove mentioned entities may benefit from. Pursuant to the provisions of the Public benefit Act public benefit activity may be carried by legal persons, entities without legal personalities which act not for profit and assign their revenues for realizing statute's goals. They do not pay out any profits to members, shareholders or employees. In order to gain the status, the organization has to fulfill listed conditions and apply for an entry to National Court Registry.

The status of public benefit organizations – as was said herein – may gain both company, association and foundation. They have to run public benefit activity in accordance with legal definition specified in the Public benefit

Act. It means activity socially useful and realizing goals in public interest<sup>7</sup>. Any business run by an organization can have only additional character. An organization is obliged to spend all revenues on public benefit activity. In order to gain the status of public benefit organization an organization has to lead an activity for at least two years.

Public benefit organization cannot be understood as a synonym of a non-profit organizations. It is important to stress that all herein described entities: companies (limited liability company and joint stock company), associations and foundations may play a role of a non-profit organization. Taking into account the structure of such entities as associations and foundations, it has to be stated that they are always the non-profit organizations. Companies have to point certain goals in their statutes in order to be recognized as non-profit organization. When it comes to term of public benefit organization, it relates to a status which all herein described entities may benefit from. The status of a public benefit organization is something extra on the top of non-profit organizations, but on the ground of the Polish tax law it is also a prerequisite to benefit from a few special tax rules. In fact it is a public benefit organization that is granted the most of tax benefits. Specific tax rules which all non-profit organizations are granted are described in the next parts of this thesis.

When it comes to international aspects of preferential treating of non-profit activity, there are different regulation depending on the status of foreign entity. As it was afore said in Polish tax law there are distinguished two types of entities which may be granted tax exemption.

The first one is entity which is exempted based mainly on the base of the purpose of activity. As long as foreign organizations fulfill all requirements of this regulation (i. a. legal personality and certain goal of the activity), they are allowed to benefit from tax exemption. Taking into account that in order to meet these conditions a foreign organization would have to possess its residence in Poland (to register in the National Court Register), it is impossible for foreign third sector to benefit from this regulation.

Nevertheless, there exists the second type of an entity - public benefit organizations – which may be granted tax exemption. This regulation refers to foreign entities explicitly. They are granted tax exemption if they possess in their residence state the status similar to public benefit

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<sup>7</sup> In order to become a public benefit organization an entity has to realize one of the purposes which are listed under art. 4 of the Public benefit act. These were exemplified in the footnote no. 5.

organization in Poland. There is also the second requirement. There must exist the mutual assistance procedure between Poland and the state a certain foreign non-profit organization comes from. In the European Union this condition is met by all Member States as a consequence of implementation of the Council Directive 77/799. The described exemption was implemented to Polish tax law after *Centro di Musicologia Walter Stauffer* case<sup>8</sup>. The amendment of Polish tax law was a result of a "reasoned opinion" which Commission sent Poland to end discrimination of foreign entities. Although the object of request was only tax exemption in the person of a donor, Poland amended all provisions referring to non-profit organizations.

There are some doubts in the Polish tax doctrine, whether these amended conditions are compliant with the European law.<sup>9</sup> It is pointed that requirements foreign organizations have to fulfill are a kind of limitation of the freedom of capital. It is also commented that in most cases one requirement would be enough to assure the control of tax authorities.

### 1.3. International organizations

On the ground of the Polish tax law there is also regulation directed to international organizations. Pursuant to the article 17 para. 1 point 23 of the CIT Act "The following items shall be free from income tax (...) income obtained by taxpayers from the governments of foreign states, international organizations or international financial institutions, from non-refundable aid funds, including the funds of framework programmes for research, technical development and presentation of the European Union and NATO programmes, granted on the basis of a unilateral declaration or agreements concluded with those states, organizations or institutions by the Council of Ministers, the competent minister or government agencies; including also the cases whereby those funds are distributed through an agency authorized to distribute non-refundable aid funds to beneficiaries"<sup>10</sup>. The provision refers to funds which legal person (e.g. a company) receives from non-resident who is non-profit organizations. The regulation covers only an example of non-refundable aid which comes from international organization. Tax authorities construe "international

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<sup>8</sup> The ECJ case C-386/04 *Centro di Musicologia Walter Stauffer* of 14<sup>th</sup> September 2006.

<sup>9</sup> Łukasz Adamczyk, *Zakaz dyskryminacji organizacji pozarządowych z państw unijnych – glosa – C-386/04 "Centro di Musicologia Walter Stauffer"*, Monitor podatkowy, no. 2, 2007.

<sup>10</sup> Art. 21 para 1 point 46 of the PIT Act.

organizations” as organizations which have international character. It means their participants come from different countries.<sup>11</sup>

It is evident that foreign non-profit organizations may benefit from the same preferential tax regulation as domestic organizations. After fulfilling certain requirements their income is tax exempted.

#### 1.4. Summary

To sum up, it has to be underlined that the Polish legislator recognizes the special role which non-profit organizations play in the society. A non-profit organization may have the legal form of a foundation, an association or even a company. Neither civil law nor tax law does not oblige to carry non-profit activities in a certain legal form in order to be perceived a non-profit organization. Nevertheless, the legal form influence possible tax benefits an organization may benefit from.

Generally, income of non-profit organization is tax exempted. However, not all entities are allowed to benefit from the exemption. There are several conditions which these entities have to fulfill. It is important to stress that qualification of an entity as a non-profit organization does not mean that it is granted all tax benefits.

Tax law distinguishes two basic income exemptions. The first refers to purpose of the activity, the second to the status of a public benefit organization. The details of rules are discussed in the following part (Part II of the thesis).

Tax benefits are not reserved only for Polish non-profit organizations. There is a special regulation which exempts income of certain no-profit organizations. Special regulation is provided for international organizations as well. Their aid to natural persons or legal persons is tax exempted.

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<sup>11</sup> The individual interpretation of the Minister of Finance from 11<sup>th</sup> February 2009 by (no. IPPB4/415-17/09-2/JS).

## 2. Income tax

### 2.1. Material conditions for special tax status

According to the general rule all entities have to pay taxes if they receive any income. In the CIT Act there are provided for a few exemptions of subjective character. On this list non-profit organizations are not mentioned. Therefore, it has to be concluded that all non-profit entities are treated as taxpayers.

Both legal acts do not distinguish the category of non-profit organization. On the ground of the CIT Act there is used simply the term taxpayer whose statutory purposes include goals which are listed in the CIT Act (see the article 17 para. 1 point 4 of the CIT Act). The only exception are public benefit organizations (e.g. the article 17 para. 1 point 6c of the CIT Act).

The basic provision which set rules of tax treatment of non-profit entities is the article 17 para. 1 point 4 of the CIT Act. Pursuant to the provision "(...) shall be free from income tax: (...) income of taxpayers, subject to paragraph 1c, whose statutory purposes include scientific, scientific-technical, didactic, educational, including teaching of students, cultural activities, activities in the field of physical culture and sports, environment protection, supporting community initiatives with respect to the construction of roads and the telecommunications network, and water supply in rural areas, charity, health protection and social welfare, occupational and social rehabilitation of disabled persons, religious cult - the part thereof appropriated for those purposes." In order to benefit from this regulation the taxpayer has to include at least one of listed goals in its statute. The catalogue of goals is closed. It means that only goals stipulated in the provision allow to benefit from tax exemption. Another requirement pointed in the provision is to appropriate certain sum of money to the same value which pointed in the statute. The provision is construed in the same way by the court. According to the Supreme Administrative Court "In order to benefit from tax exemption set forth in the article 17 para. 1 point 4 of the CIT Act the entity has to fulfill two requirements: its statute's aim has to be activity compliant with this provision and obtained income has to be spent on this aim."<sup>12</sup> What is important, a goal has to be stipulated in a statute very precisely.

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<sup>12</sup> The judgment of Supreme Administrative Court from 3<sup>rd</sup> October 1995 (SA/Wr 1283/95).

According to administrative authorities "Goals of association ought to be defined in the statute. They have to be pointed precisely, because administrative authorities are not allowed to construe them. The administrative authority has to examine, if goals from the statute are the same as those listed in the CIT Act. Legal provisions which constitute tax exemption are the exception of the equality rule in taxation. Therefore, extensive interpretation cannot be applied."<sup>13</sup>

Although the provision seems to be simple, the practice raise many questions. In the regulation it is not defined whether this specific goal has to be the only goal of the entity. As the jurisprudence explained, "the article 17 para. 1 point 4 of the CIT Act does not require that stipulated in the provision aims have to be the main or the only goal of entity's activity."<sup>14</sup> It means that the statute of a certain entity may provide for different kinds of goals. However, tax exempted income will be only this part of the whole income which are appropriated for the purpose stipulated in the analyzed provision.

According to the part of doctrine<sup>15</sup>, the relation between the appropriation of the income and its spending does not have to be direct. It means that those spending which fulfill certain goals only indirectly may be tax exempted as well. The example may be purchase of a car for an employer of an entity.

It should be also noticed that pursuant to the article 17 para. 1 point 4 of the CIT Act certain income does not have to be spend on financing activity which realizes the purpose pointed in the regulation. Tax exemption will be also allowed when the income will be spent on supporting this kind of activity. This interpretation of the regulation is presented by tax authorities. According to the Minister of Finance: "The phrase *whose statutory purposes include* should be understood not only as direct keeping education activity but also as supporting it if it is the goal stipulated in the statute of this entity."<sup>16</sup>

The CIT Act provide for two sorts of exceptions from the analyzed regulation. The first exception regard the source of income which regardless of the purpose of appropriation cannot be tax exempted.

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<sup>13</sup> The decision of Minister of Finance in Bialystok from 22nd March 2007 (RO-XV/423/PDOP-35/ 54/07/JB).

<sup>14</sup> The judgment of Supreme Administrative Court from 28 February 1996 (SA/łd 1997/95).

<sup>15</sup> A. Mariański K. Nykiel, *Komentarz do ustawy o podatku dochodowym od osób prawnych*, Gdańsk 2010, p. 791.

<sup>16</sup> The letter of Minister of Finance from 16<sup>th</sup> March 1995 (PO 4/P-722-265/95).

Pursuant to the article 17 para. 1a of the CIT Act this is "income from commercial activities consisting in manufacturing of electronic products, fuels, tobacco products, spirits, wines, beers, as well as other alcoholic beverages with alcohol content of more than 1,5%, as well as products made of precious metals or including those metals, or trading in those products". It has to be underlined that this exclusion does not cover the income of scientific and research and development facilities, within the meaning of separate regulations, from activities consisting in manufacturing of electronic products. Another type of income, which is excluded from the benefit of the article 17 para. 1 point 4, is income from leasing assets or intangible assets. The last group of income relates to income (regardless of the time it was generated) which was expended on purposes other than pointed in the analyzed regulation. In this way, it is eventually decided that income of the entity does not have to be only appropriated on the specific purpose but it has to be also spent on the same purpose. In the same time the legal act distinguishes two important moments for the taxpayers – the moment of appropriation and the moment of expending. There has to be the same purpose (the one stipulated in the article 17 para. 1 point 4 and the same in the statute) at the both moments. Only then is taxpayer allowed to benefit from tax exemption with reference to this part of income. On the other hand, analyzed exceptions indicate that sources of income which are different to those in art. 17 para. 1a of the CIT Act, may support non-profit activity without losing by organization tax benefits. In fact funds from any kind of activity which are different to herein discussed do not deprive non-profit organization of tax exemption. The most important factor which influences tax treatment of non-profit organizations is the purpose funds are spent on.

Another sort of exclusion from tax exemption is of subjective character and relates to certain group of taxpayers. These taxpayers are: state-owned enterprises, cooperatives and companies, incorporated municipal companies, for which the function of the founding body is performed by local government units or their subsidiary entities established pursuant to separate regulations and budgetary establishments and other unincorporated organizational units which pay corporate incomes tax - if the object of their activities is to satisfy public needs indirectly linked with environmental protection with respect to: water supply and sewage systems, municipal sewage, waste dumps and municipal waste management and its collective transport.

The analyzed regulation seems to be clear. If a taxpayer included in its statute certain goals stipulated in the article 17 para. 1 point 4 of the CIT Act and appropriated its income on this goal, the income will be tax exempted. The regulation may be applied by any legal form which meets these conditions. The subjective exclusion has to be taken into account.

In the CIT Act there is another regulation which exempts income in reference only to certain not only activity but also entities. Pursuant to the art. 17 para. 1 point 4 of the CIT Act tax exempted is income received by public benefit organization which is appropriated on statute activity, with exception of business activity. This exemption is not limited by goals which should be stipulated in the statute and by the source of income which should be spent on. The provision sets forth general tax exemption which is granted public benefit organizations. The only exclusion in this wide regulation is spending income on business activity. This part of income cannot be tax exempted.<sup>17</sup>

## 2.2. Formal conditions for special tax treatment

Special tax treatment of the most of non-profit organizations is strictly connected with some formal conditions which has to be fulfilled. It is obvious that being a foundation, an association or having the status of public benefit organization is not enough to claim special tax treatment.

First of all, it has to be underlined that tax exemption which especially public benefit organization benefit from does not exclude the obligation to register as a taxpayer. According to the practice of tax authorities, non-profit organization are taxpayer, even if they are tax exempted. Therefore, they have to move for the number of tax identification. In this way, they start to exist in the register of tax authorities.<sup>18</sup>

Pursuant to the art. 27 para. 1 of the CIT Act the taxpayers are obliged to file a tax return till the end of the third month after the end of tax year. In special annexes the non-profit organization has to declare income which is exempted on the ground of the tax exemption stipulated in the art. 17 para. 1 point 4 (the exemption of income which is spend for the statute purposes), income which is exempted on the base of the status of public benefit organizations (excluding business income). A non-profit

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<sup>17</sup> M. Supera-Markowska, *Podatkowe aspekty działalności organizacji pozarządowych (I)*, Prawo i Podatki, no. 12, 2009.

<sup>18</sup> The individual interpretation of Minister of Finance from 22nd January 2008 (ILPP1/443-359/07-2/BD).

organization has to submit a list of all donors who in tax year made a single donation of not less than 15.000 PLN. This obligation refers also to donors whose total value of donations in tax year was not less than 35.000 PLN. The list has to be made public e.g. on the Internet. Entities which has income lower than 20.000 PLN does not have to publish these materials.

Moreover, there are provided for special duties only for public benefit organizations. They are strictly connected with the income deduction which donors may benefit from (it is described in the subpart 2.10). In accordance with the regulation a beneficent of donation is obliged to single out from revenues the total amount of donations received and make it available information for public knowledge.

### 2.3. Income from purely non-profit activities

Polish tax law does not distinguish the term of purely non-profit activity. The tax exempted income is this one which meets certain requirements describe in the regulation in CIT Act (herein above discussed).

Nevertheless, it is worth mentioning that all tax acts distinguish three types of activity: business activity, no gratuitous statute activity, gratuitous statute activity. No gratuitous statute activity and gratuitous statute activity are not for profit activities in contrast to business activity which is typically for profit. Income tax acts do not take into account the source of income of non-profit organization as long as it is not the one described in the commented art. 17 para. 1a of the CIT Act. The influence of kind of activity on possibility to benefit from tax exemption is a feature of e.g. an estate tax or a civil acts tax.

### 2.4. Business income used to support non-profit activities

As it could be noticed in the analysis presented in the subpart 2.1 of this thesis, generally the source of income does not influence the right to benefit from tax exemption by public benefit organization or any other non-profit organization. The only limitation is provided in the art. 17 para. 1a. It was also commented in the subpart 2.1.

At this point it is worth mentioning the exemption of income received by companies which the only partner is an association. In other words, Polish tax law recognizes income of company which is hold exclusively by an association as tax exempted. The provision includes two more conditions.

The holding association has to put in its statute one of goals stipulated in art. 17 para. 1 point 4 of the CIT Act. The income of the hold company must be appropriated on this goal and transferred to the holding association. According to tax authorities, a company which is mentioned in the provision must be a legal person. Partnership are not allowed to benefit from the regulation.<sup>19</sup>

From the perspective of the European law there is the question whether foreign association which would set up a company in Poland could benefit from tax exemption. The analyzed provision refers only to associations which are established on the ground of the Law on associations. There is no rule of mutual recognition in this respect. So far this issue was not construed by tax authorities or administrative courts.

Another very interesting regulation refers to income derived from shares in legal persons. This income may be also exempted. A non-profit organization has to meet two requirements: the first one refers to appropriation of income to purposes stipulated in its statute (the purposes listed in the art. 17 para. 1 CIT Act) and the second refers to information send to a withholding agent regarding benefiting from exemption.

## 2.5. Investment income used to support non-profit activities

It is obvious that most of entities expand not all of its income. It is quite often that reasonable manager tries to increase the budget of the entity. Therefore, income is quite often reinvested. The question regarding investment income arises.

There are possible different ways of investing money. The most often entities purchase bond and other different securities. It raises the question whether such expansion of the income benefits from the article 17 para. 1 point 4 of the CIT Act. This aspect of non-profit activity was the legal problem in Poland through a few years. The issue was the object of the dispute in Supreme Court in 2002.<sup>20</sup> According to the court, the purchasing of bonds is only intermediary fact which does not carry any deeper sense from tax perspective. In fact when an entity decides to buy any stocks, it does not change the purpose of appropriation of this money. The entity only does insure its income. By purchasing any kind of stocks it

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<sup>19</sup> The individual interpretation of the Minister of Finance from 11<sup>th</sup> December 2008 by (no. ILPB3/423-781/08-2/HS).

<sup>20</sup> The judgment of the Supreme Court from 13<sup>th</sup> March 2002 (III ZP 21/01).

does not consume the income which still may be expended on purposes compliant with a statute. In this way the court distinguished three types of acts: appropriation, allocation and spending. Allocation is a completely different act from spending. Therefore, the income which a foundation allocate and buy securities does not exclude spending this income on goals pointed in a statute.<sup>21</sup>

After this well known in Polish doctrine judgment the legislator decided to amend the provision of the CIT Act.<sup>22</sup> In 2004 there was introduced a new provision art. 17 para. 1e of the CIT Act. The regulation introduced tax exemption only for a certain type of allocation of income. Pursuant to the provision tax exempted is allocation of income which consists in acquiring bonds (issued by the State Treasury after 1 January 1989 or bonds issued by local government units after 1 January 1997), securities and financial instruments, participation units in investment funds (operating pursuant to the provisions of the Act of 27 May 2004 on Investment Funds (Dz.U. No. 146, item 1546)). In case of securities, the regulation covers only securities other than allowed for public trading, providing they have been purchased with respect to management of third party's securities portfolio on commission, referred to in Article 30.2.4 of the Act of 21 August 1997 on Public Trading in Securities (Dz.U. of 2002 No. 49, item 447 and No. 240, item 2055 and of 2003 No. 50, item 424 and No. 84, item 774), on conditions that those securities have been deposited in a separate account kept by an authorized entity. The new regulation has been strongly criticized. As it is pointed in the doctrine<sup>23</sup> instead of implementing the findings of Polish tax jurisdiction, the legislator diminished the scope of tax exempted acts. The amendment points that only selected acts may be the subject of preferential regime. It means that all other are not covered by the scope of the exemption. In case a non-profit organization purchased bonds, the income allocated in bonds would be tax exempted. If it opened a deposit, it would have to pay tax. It is hard to understand the rationale which lies behind this distinction. The regulation leads to situation when an organization has to spend cash or allocate it in the way pointed in the provision. Opening a deposit account would take effect of taxation.

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<sup>21</sup> K. Szczepański, *Fundacja – jednak bez podatku*, *Vademecum Doradcy podatkowego*.

<sup>22</sup> A. Mariański, *Opodatkowania organizacji pożytku publicznego*, *Przegląd podatkowy*, no. 1, 2004.

<sup>23</sup> A. Mariański, W. Nykiel, *Komentarz*, p. 788.

The amendment of the CIT Act does not solve the problem of investment income and possibility to invest money by non-profit organization. It was in 2009 when the Supreme Administrative Court stated that before 2004 (implementing new provision) non-profit organization were not allowed to benefit from tax exemption in reference to money which are invested e.g. in shares of companies.<sup>24</sup> According the court, the amendment of the CIT Act means that before this time, this income should have been taxed. This interpretation is not in line with judgment from 2002 (commented herein above). Nevertheless, the judgment gain recognition of the tax law doctrine<sup>25</sup>.

## 2.6. Remuneration or reimbursement of expenses

In order to achieve its goals, non-profit organization may be an employer. There are no special treatment of non-profit organizations on this ground. Both labour law and tax law set the same obligations as in case of typical profit entities.

On the ground of tax law it means that each month non-profit organization has to pay tax advance for income tax of its employees. After the end of the year non-profit organization is obliged to set a declaration for its employees. In declarations there are information about tax advances which were paid by employer.

There are also no special tax rates or other allowances for employees of non-profit organization. A non-profit organization is not only a payer of tax advances but also a payer of contribution to national insurance.

The only exception are not-profit organizations which have a status of the public benefit organization. Although public benefit organizations are obliged to follow the general rules, they are limited in the scope of the remuneration. If a public benefit organization pays a remuneration which exceeds three times the average month remuneration in Poland during the time of the last three months, it is qualified as the one that runs business. That is why, a public benefit organization in order not to be qualified as running business activity has to set salaries of its employees carefully.

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<sup>24</sup> The judgment of the Supreme Administrative Court from 16<sup>th</sup> October 2009 (II FSK 1654/2007).

<sup>25</sup> R. Mastalski, The approving gloss, OSP 2010/10, p. 744.

## 2.7. Tax treatment of public subsidies in the tax base

A non-profit organization may be financed from different sources. It is not only income from own business or investments that may support non-profit activity. Public subsidies are also a very important source. This special kind of financing non-profit organization is separately regulated in the Polish tax law. The general rule is that public subsidies are tax exempted income of non-profit organization. Polish income tax law distinguishes three types of income within public subsidies which are tax exempted. They are income obtained from non-refundable aid funds, subsidies obtained from national budget or budget of local government and income obtained from government agency.

Pursuant to the art. 17 para. 1 point 23 of the CIT Act tax exempted is income which is obtained by taxpayers from the governments of foreign states, international organizations or international financial institutions, from non-refundable aid funds, including the funds of framework programmes for research, technical development and presentation of the European Union and NATO programmes, granted on the basis of a unilateral declaration or agreements concluded with those states, organizations or institutions by the Council of Ministers, the competent minister or government agencies. It includes also cases whereby those funds are distributed through an agency authorized to distribute non-refundable aid funds to beneficiaries. This provision is discussed in the first part of this thesis. What is however worth stressing here, the regulation covers the aid funds granted by not only international organizations but also by foreign governments. In this way this funds may be treated as public one.

National subsidies which are understood as obtained from national budget or budget of local government are the second type of income within public subsidies. Pursuant to the art. 17 para. 1 point 47 of the CIT Act tax exempted are subsidies obtained from national budget or budget of local government. Surcharges to interests rates in bank loans are the exception.

The income obtained from government agencies or executive agencies which obtained financial means from national budget are the third source of subsidies which is tax exempted (art. 17 para. 1 point 48 of the CIT Act).

These three provisions create complete system of tax exempted subsidies which non-profit organization may be granted. What is interesting, any of

indicated provisions does not stipulate the purpose the subsidy should be allocated for. The rationale for such a legislation may be found the institution of subsidies. Generally, in order to be granted any of them, the applicants have to meet several conditions. The whole procedure is usual very complicated and consists of a few stages. Mostly, the whole process of spending subsidy is still under control of entity which grants subsidy. It raise the question whether subsidy spent on different than anticipated purpose will be still tax exempted. The lack of regulation in this scope opens areas for tax abuse.

Another doubts refer to limitation of the granting entities to international entities. Foreign or domestic organizations are not allowed to grant tax exempted subsidies.

## 2.8. Accumulation of income

Polish tax law do not provide for any special tax treatment of accumulation of income. However, some consideration may be found in the subpart 2.2 commenting investment income.

## 2.9. Liquidation of a non-profit organization

Any non-profit organization may be dissolved. In this case there are no special tax treatment of assets or any other property that is released after dissolution. In order to clarify tax consequences, general rules have to be taken into account.

Pursuant to the CIT Act property received in reference to liquidation of legal person (in cash or in kind) is treated as an income from the participation in legal persons. It is taxed at tax rate of 19%. However, there are possible some exemptions. In fact they depend on legal form of a non-profit organization.

If a non-profit organization acts as a foundation, there is special regulation provided. Pursuant to the Act on foundations, there are only two cases when a foundation may be liquidated. The first one relates to achievement of the purpose the organization was established for. The second one relates to exhaustion of its financial assets. Generally, the foundation's status should prescribe the procedure for dissolution. If there is no procedure in a statute, it is a court that decided about the liquidation of a foundation. The Act on foundations provided for that a court appropriates assets of the entity taking into account the purposes the

organization was established for. In other words, if a purpose of a foundation which is wound up is supporting orphanages, there is a high possibility that the court appropriates the property of this foundation on this purpose. If assets of this foundation will be appropriated by the court for another foundations which statute's purposes will be identical to those of a liquidated organization, no tax will be paid. It is a consequence of subjective tax exemption described in the subpart 1 of this thesis.

In case of associations, the provisions of the Law on associations provided for special procedure as well. If an association is liquidated, assets of an association should be appropriated in reference to the provisions of a statute or a special resolution of the association. If there is neither provisions in a statute nor a resolution referring to this matter, it is a court that appropriates assets for specified public purpose. If this purpose is identical to purposes of the liquidated association, the non-profit organization is not liable to pay tax (pursuant to subjective tax exemption described in the subpart 1 of this thesis).

Similar tax consequences may be noticed when considering public benefit organizations. It means that, if during the procedure of liquidation, all assets of a public benefit organization are appropriated in reference to the purpose of this organization, no tax is liable.

There may arise the question what tax consequences arise when a company hold only by an association is wound up. According to tax authorities, if a whole property is transferred to a holding association, a company is not obliged to pay any tax.<sup>26</sup>

## 2.10. Deductions of gifts and contributions

The preferential regime of taxation is provided also for donators who contribute to existence of non-profit sector. Special provisions are stipulated both for legal persons in the CIT Act and natural persons in the PIT Act. In both tax acts there are provided similar institutions. Therefore, they are discussed jointly.

In the PIT Act there are provided three institutions regarding donations to non-profit organizations. The first one is possibility to deduct tax due, the second to deduct a tax base and the third one allows to treat some

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<sup>26</sup> The individual interpretation of the Minister of Finance from 23<sup>rd</sup> February 2011 by (no. ILPB4/423-312/10-4/ŁM).

expenses as deductible costs. In the CIT Act there are stipulated only two last institutions.

As was afore said, the deduction of tax due is allowed only on the ground of the PIT Act. It provides for possibility to reduce due tax by 1%. It means that a taxpayer instead of paying 100% of his tax due, may pay only 99%, if he make a donation of 1% to a public benefit organization. Pursuant to the art. 45c para. 2 of the PIT Act a taxpayer may benefit from the deduction, if he pays due tax not later than in two months from day the tax return has to be filed. It is worth mentioning that a taxpayer do not make donation himself but it is made by tax authorities in reference to tax return. In tax return a taxpayer may choose whether he want to make a donation or not. Non-profit organizations that may benefit from regulation are only public benefit organizations.

The second institution which is common for the CIT Act and the PIT Act refers to the income deduction. This regulation also concerns situation where a beneficent of donation is public benefit organization or is its counterpart acting within the European Union or European Economic Area. The subjective scope of this deduction is wider than in case of tax deduction. Pursuant to the provision art. 18 para. 1 of the CIT Act (art. 26 para. 1 point 9 of the PIT Act) the taxable base may be deducted by donations for the purpose of public benefit organization and donations for the purposes of religious cult. The PIT Act provides for deduction for the purpose of blood donation as well. The described institution allows the taxpayer to make deduction which does not exceed in the tax year the amount corresponding to 10% of income. In the PIT Act the deduction cannot exceed 6% of income. It has to be stressed that the percentage refers to donations for the purpose of religious cult and for the purpose of public benefit organizations jointly (in case of the PIT Act it refers also to blood donation). In other words the total amount of deductions for these purposes cannot exceed 10% (or 6% in the PIT Act) in the tax year.

It is obvious that there may be sundry objects of donation. Therefore, it has to be pointed that in case a donor make a donation in the form of some goods or service, the value of donation is calculated as a gross value (including VAT tax). However, a donor is allowed to include into account only this part of input tax, which a donor cannot decrease when realizing his right of deduction on ground of VAT Act.

Both acts (the CIT Act and the PIT Act) provide for subjective exclusion of some entities. Pursuant to the art. 18 para. 1a of the CIT Act (art. 26

para. 5 of the PIT Act) donation made in favour of natural persons or legal persons or unincorporated organizational units conducting commercial activities consisting in manufacturing of electronic products, fuels, tobacco products, spirits, wines, beers, as well as other alcoholic beverages with alcohol content of more than 1,5%, as well as products made of precious metals or including those metals, or trading in those products cannot be deducted.

The analysis of tax treatment of gifts and donations in the person of donor or contributor has to include formal conditions which has to be met in order to benefit from income deduction. First of all, a donator has to indicate in the tax return the amount of the donation transferred, the amount of the deduction made and data allowing for identification of the beneficiary, in particular their name, address and tax identification number. Secondly, any donation has to be determined on the basis of documents certifying their incurrence. If a donor makes pecuniary donation, the relevant document is a receipt documenting payment to the bank account of a beneficiary. In case of donation other than in cash a relevant document is any paper stating the value of that donation, data of a donor and a beneficiary's declaration of its acceptance. Regarding the blood donation, set forth in the PIT Act, the relevant act is a certificate documenting the amount of blood donated. The last category of donation stipulated in tax law is material or service donation. The document has to include information regarding data of a seller, data of a purchaser, a kind of good or service being the object of a sale and the price.

Polish income tax law does not only provides for the possibility of deductions of the tax or income. Another regulation which is worth mentioning regards donations as tax deductible costs.

Generally, gifts and contributions are not tax deductible costs. Nevertheless, if a businessman, who is a VAT taxpayer, produce or purchase any groceries which later on are granted public benefit organization for its charitable purposes, the cost of producing or purchasing of such a product is a tax deductible cost<sup>27</sup>. It is vital to stress that in case a donor treats these groceries as tax deductible cost, he cannot benefit from income deduction. The ratio is that the same value cannot be deducted twice.<sup>28</sup>

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<sup>27</sup> The art. 16 para 1 point 14 of the CIT Act or the art. 23 para. 1 point 11 of the PIT Act.

<sup>28</sup> M. Supera-Markowska, *Podatkowe aspekty działalności organizacji pozarządowych (II)*, Prawo i Podatki, no. 1, 2010.

### 3. VAT cases

The regulation of value added tax (VAT) in Polish tax law is the effect of harmonization of this tax in the European Union. The national provisions are more or less the copy of the VAT Directive. Therefore, it is necessary to point general concept of non-profit activity on the ground of the VAT Directive and eventually explain certain deviations on national level.

#### 3.1. Material conditions of special VAT status

The VAT Directive does not regulate non-profit activity expressly. Under art. 9 of the VAT Directive the term of "taxpayer" means *any person who, independently, carries out in any place any economic activity, whatever the purpose or results of that activity*. Knowing that economic activity is opposition of non-profit one, it is obvious that typical activity of the third sector is out of scope. However, it happens that non-profit organization sometimes perform economic activities as auxiliary ones. Therefore, non-profit organizations that perform business activity or chargeable statutory activity are qualified on the ground of the VAT Directive (and VAT Act) as taxpayers.

Analyzing provisions of the VAT Directive and the VAT Act it is necessary to remember that the right to deduct tax is allowed only then when a taxpayer could recover input tax. It means that in most situation a non-profit organization which is not allowed to recover input tax, cannot charge output tax.

When it comes to donors who supply services out of charge, they also will not be obliged to charge output tax. Under the art. 8 para 2 of the VAT Act services which are out of charge, supplied not in reference to running business and a taxpayer is allowed to deduct tax from previous transaction are qualified as payable services and taxed. Polish taxpayers apply this provision when supplying services to non-profit organizations. They just explain that their service is out of charge but strictly connected with their business (e.g. it improves their reputation). In this way they are allowed to deduct output tax and do not have to count input tax. This interpretation of provisions was confirmed by jurisprudence.<sup>29</sup>

Not only is there a few particular legal solutions how to avoid charging input tax, but there are provided for some objective exemptions as well.

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<sup>29</sup> The judgment of Supreme Administrative Court from 23<sup>rd</sup> March 2010 r., I FSK 326/09.

In the VAT Directive there is the special group of tax exemptions which is without right to deduction and concerns activities exempted in the public interest. Most of provisions are restricted to supplies by bodies governed by public law. Under the art. 132 of the VAT Directive only three exemptions are directed to non-public bodies. The first exemption refers to the supply of services by independent groups of persons for the purpose of rendering their members the services directly necessary for the exercise of that activity. The second relates to the supply of services, and the supply of goods closely linked thereto, to their members in their common interest by non-profit organizations with aims of a political, trade-union, religious, patriotic, philosophical, philanthropic or civic nature. The last one regards the supply of certain services closely linked to sport or physical education by non-profit-making organizations to persons taking part in sport or physical education. In this scope Polish tax law provides the same type of exemptions. They are provided for in the art. 43 para. 1 of the VAT Act. They do not deviate from the exemptions specified in the VAT Directive. The only disparities lies in the exemptions of services linked to sport or physical education. As European legislator does not specify that all services are to be exempted but only certain, therefore Polish legislator limited the scope of exempted services. Services linked to marketing, advertising, promotion, entrance to sport events, sport shipping, accommodation linked to sport activities, renting sport equipment or sport buildings are excluded from exemption. What is more this exemption provides for special condition. Organizations has to put into their statute that their purpose is activity for development and publicizing of sport. This condition is not provided for in the VAT Directive.

In all two last exemptions (political services and sport services) there are provided for a few other conditions both under the VAT Directive and the VAT Act. Non-profit organizations in order to benefit from these rules cannot perform these services as systematical way of making profit. Arising profits should be assigned to the continuance or improvement of the services supplied. A service or supply of good cannot distort competition, such as to place at a disadvantage commercial enterprises which are subject to VAT. These acts have to be necessary for performing the basic service (necessary to realize the purpose of an organization).

The criterion of necessity of service in connection to realizing the purpose of the association is the source of controversy. The question refers to a membership fee which is paid by members of associations. Some tax authorities point that this fee may be tax exempted only in the case when

an association provides a service in reverse for fee and this service is not directly connected with the exempted purposes.<sup>30</sup> According to existing opinion of the Court of Justice of the European Union membership fee should not be taxed, if it is appropriated for statute purposes and members of an association do not affect it.<sup>31</sup> Polish administrative courts do not qualify membership fees as taxed as well.<sup>32</sup> The reason for it is the link between this fee and the possibility to join an association.<sup>33</sup> Nevertheless, in the last time there appeared the new approach towards membership fees. The Polish jurisprudence paid attention to the role which an association may play. If it acts as e.g. an intermediary, its activity should be treated as a service and therefore should be taxed.<sup>34</sup> Each case has to be judged individually.

Other activities which are exempted from taxation are those which are carried in areas of medical care, public assistance or cultural services. Under Public benefit Act they may be also performed by the third sector.

The described exemptions are strictly linked to the purpose of activity. The VAT Directive provided for also other exemptions which depends only on annual value of sales. It is so-called exemption for small enterprises. If annual value of sales does not exceed 30.000 EUR<sup>35</sup>, a taxpayer that runs business may be tax exempted. This right is the choice of a taxpayer. The annual value of sales which is taken into account does not include supply of goods and service for consideration which are tax exempted as well as the value of these goods which, under income tax regulations, are included by the taxpayer in his tangible and intangible assets subject to amortization. In the moment the value of sales exceeds 30.000 EUR, exemption is no longer in force. Tax obligation arises in this moment. If organization runs business activity and does not exceed specified limitation of 30.000 EUR, it does not have to register as a VAT taxpayer.

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<sup>30</sup> The individual interpretation of Minister of Finance from 26<sup>th</sup> August 2011 (IBPP1/443-853/11/LSz).

<sup>31</sup> The judgment of the ECJ from 8<sup>th</sup> March 1988, no. C-102/86, *Apple and Pear Development Council v. Commissioners of Customs and Excise*.

<sup>32</sup> E. Rogala, VAT od statutowej działalności organizacji i stowarzyszeń, online: <http://finanspubliczne.bdo.pl/biuletyn/59/daniny-publiczne/zwolnienia-od-vat-statutowych-uslug-organizacji-czlonkowskich-w-nowym-swietle.html>.

<sup>33</sup> The judgment of the Supreme Administrative Court from 30<sup>th</sup> August 2000 (947/98), the judgment of the Voivodship Administrative Court from 18<sup>th</sup> September 2006 (III SA 1976/06).

<sup>34</sup> The judgment of Supreme Administrative Court from 10<sup>th</sup> September 2011 (I FSK 1215/10).

<sup>35</sup> The art.113 of the VAT Act.

The lack of tax obligation does not influence the duty to run records and file VAT declaration.<sup>36</sup>

Tax practice proves that very often organizations which benefit from exemption for small enterprises exceed the limitation. There are some doubts whether they should qualify as VAT taxpayers, if after exceeding this limitation they claim undertaking VAT acts only occasionally. According to Polish tax authorities, even than non-profit organization should register as a VAT taxpayer.<sup>37</sup>

### 3.2. Formal conditions for special VAT status

Under the art. 9 of the VAT Directive the status of taxpayer is strictly linked to performing economic activity. It is obvious that if a non-profit organization does not run business, there is no formal conditions it has to meet.<sup>38</sup> The situation changes when it starts to perform exempted or taxed activities.

Under art. 272 of VAT Directive Poland exempts taxable persons carrying out only supplies of goods or of services which are exempted pursuant to Articles 132 and taxable persons covered by the exemption for small enterprises. These entities may register as exempted VAT taxpayers. Therefore non-profit organization which benefits from exemption for small enterprises or perform exempted activities (pursuant to the art. 43 para. 1 of the VAT Act) does not have to register as a VAT taxpayer. However, they may register as an exempted VAT taxpayer. In the moment of exceeding the limitation for small enterprises, an organization is obliged to register as a VAT taxpayer. A non-profit organization which meets requirements for small enterprises exemption is always allowed to resign from it.

This interpretation of VAT Act was confirmed by tax authorities.<sup>39</sup>

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<sup>36</sup> M. Supera-Markowska, *Podatkowe aspekty działalności organizacji pozarządowych (III)*, Prawo i Podatki, no.. 2, 2010.

<sup>37</sup> The individual interpretation of tax provisions from 13th February 2009 by Minister of Finance (IPPP1/443-2086/08-2/IG), the individual interpretation of tax provisions from 17<sup>th</sup> May 2010 by Minister of Finance (ITPP2/443-198a/10/RS).

<sup>38</sup> K. Różycki, *Stowarzyszenia i fundacje jako podatnicy VAT*, Vademecum Doradcy Podatkowego, 2010.

<sup>39</sup> The individual interpretation of tax provisions from 20<sup>th</sup> October 2010 by Minister of Finance (ILPP1/443-859/10-4/NS), the individual interpretation of tax provisions from 30<sup>th</sup> August 2010 by Minister of Finance (IPPP2/443-410/10-4/RR).

### 3.3. Special rules with respect to the operation of the VAT exemption

On the ground of the Polish tax law there are provided special provisions with respect to the operation of the VAT exemptions stipulated in the VAT Directive and VAT Act. These are directly designed for public benefit organizations.

Under §13 of the VAT Ordinance tax exempted is *inter alia* supply of goods carried out by public benefit organizations. In order to benefit from the exemptions goods have to be acquired by organizations as donation coming from fund-raising.<sup>40</sup> Their market value has to exceed 2 000 PLN. The purchase has to be documented with invoice or other document allowing identification of a donor.

In the VAT Ordinance there is also provided exemption of so-called services with increased fee which are performed for a fund-raising. This exemption is linked to many additional conditions which have to be met in order to benefit from it. Public benefit organizations which is the only addressee of this exemption has to conclude a contract with supplier of public telecommunication services. Transaction has to be documented with an invoice. The purchaser of the service is informed which part of the fee is to be paid to a public benefit organization and which is the cost of the service.

The supply of goods is one of taxable transactions. The VAT Directive does not distinguish whether goods are supplied to or by non-profit organizations. Under the art. 72 of VAT Directive tax base is the purchase price of the goods or in the absence of a purchase price, the cost price.

From the perspective of contributions by business entities to non-profit organizations this regulation is assessed as disadvantageous. Although in the moment of making a gift goods lost their business value, they has to be taxed. On the ground of Polish legislation there is provided for the exception from this rule. Under the art. 43 para. 1 point 16 of the VAT Act tax exempted is the chargeable supply of grocery by a producer to a public benefit organizations (only). The object of supply cannot be e.g. alcoholic beverages which include more than 1,2% of the alcohol or mixtures of beer and non-alcoholic beverage which include more than 0,5% of alcohol. This exemption is intended to encourage producers to

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<sup>40</sup> Not all fundraises. Only regulated in the ACT on public fundraises from 15<sup>th</sup> March 1933 (Dz. U. Nr 22, poz.162 z późn. zm.).

make contributions to public benefit organizations for the charitable purposes.

When analyzing non-profit organizations it is obvious that most of them perform not only the one type of activity (exempted or not exempted) but partially chargeable activities and partially exempted. In this situation an organization is obliged to point separately sum of output tax which may be deducted. If the separation of chargeable and exempted sums is not possible, a taxpayer has to count a proportion of turnover from chargeable activities in all activities undertaken during the previous year. The sum of output tax which is calculated by using this proportion may be deducted. Activities which are not taken into account are supply of goods and services which qualify under the regulations on income tax as tangible and intangible assets subject to amortization, as well as land and rights of perpetual usufruct of land, where they are included in the taxpayer's tangible assets - used by the taxpayer for the purposes of his activity. Taxpayers cannot include into calculation turnover from transactions which refer to real estates or services exempted under the provisions of the VAT Act (pursuant to art. 43 para. 1 point 37-41), if these activities are undertaken occasional. If the proportion exceeds 98% and the calculated output tax which cannot be deducted is lower than 500 PLN (about 100 EUR), it is deemed as if a proportion would be 100%. If this proportion does not exceed 2%, it is deemed as if a proportion would be 0%.

#### 3.4. Cross-border services or supply of goods

Cross border activity of non-profit organizations is also regulated in the provisions of VAT legislation (the Directive and the national act). Non-profit organization may receive money in the form of grants or acquire some goods. Hereinafter are described tax consequences of both.

Grants from international but not only organizations stand for quite important part of financing the non-profit organizations. On the ground of the VAT there arises always the question whether non-profit organization is allowed to present its expenditures (which are donated) as the net or gross value. If a non-profit organization is a VAT taxpayer, it is allowed to deduct tax and may present its expenditure in the gross values. In order to deduct input tax, one more condition has to be met. The donation has to have direct influence on the price of goods or services they appropriate for.

Another question which refers to cross border transactions is, what are the rules of charging import transaction. In the Polish VAT Act there are three provisions which are the most relevant to non-profit organizations on this ground.

The first of them refers to rather medical help sent cross border. Under art. 62 of the VAT Act import of medicines (and other sanitary and cleaning products), goods sent gratuitously by persons having their place of residence or registered office within the territory of a third country, designated for social organisations or organisational units statutorily appointed for charity work or humanitarian aid and office supplies sent gratuitously by persons having their place of residence or registered office within the territory of a third country, designated for social organisations or organisational units statutorily appointed for charity work or humanitarian aid, used only for such activity are tax exempted. These goods cannot be alcoholic beverages, tobacco and tobacco products, coffee and tea, means of transport (with the exception of ambulances). This exemption shall apply only to such social organisations or organisational units, whose accounting procedures allow monitoring of the use of exempt goods.

The second exemption refers to goods for social rehabilitation (goods specifically adapted for the purposes of social, occupational and medical rehabilitation, and educational and cultural aid).

The last exemption covers performance of humanitarian aid. They are goods imported by state organisational units, social organisations or organisational units statutorily designated for charity work or humanitarian aid or imported by rescue units. This exemption also shall apply only to such social organisations or organisational units, whose accounting procedures allow monitoring of the use of exempt goods.

If any of these goods (referring to all three import exemption) would be used for other purpose, they would be taxed taking into account their customs value established for this day by the customs authority. There are also a few other conditions to be met.

#### 4. Inheritance, estate and gift taxes

Donations and inheritances play quite vital role in financing non-profit organizations. It is relatively often that a foundation is established as a result of the last will and its whole possession comes only from the inheritance. On the other hand, non-profit activity as a socially acclaimed often is subject of donations. Therefore, the tax consequences of these acts cannot be disregarded.

Inheritance, estate and gift taxes are regulated in Poland by two legal acts. Inheritance and gift taxes are defined by Inheritance and gifts tax Act, whereas estate taxes by Law on taxes and local levies. In order to point out specific conditions of non-profit activities on the ground of these two acts, it is necessary to focus on their scope of regulation.

In accordance with the Inheritance and gifts tax Act the object of taxation is acquisition of equity by natural persons. The legal form of acquisition which is within the scope of this Act is legally stipulated. Pursuant to art. 1 para. 1 of the Inheritance and gifts tax Act it should be donation, inheritance, testamentary legacy or further legacy, acquisitive prescription, usufruct and easement which are free of charge and a few other set forth in the provision. What is more, the Inheritance and gifts tax Act is effective only in case when a purchaser is a natural person. It means that non-profit organizations do not fall into the subjective scope of the Inheritance and gifts tax Act. As it was afore mentioned (*vide*: Part I) non-profit organizations may be run only in the form of legal persons. The result of such legal regulation is lack of taxation of any kind donations, gifts or inheritance which each non-profit organization may acquire. What has to be underlined, for the purpose of the Inheritance and gifts tax Act the residence of non-profit organizations is of no importance. Similarly, the non-profit organization does not have to possess the status of public benefit organization. The only prerequisite is the legal personality. This interpretation of tax law is confirmed by tax authorities<sup>41</sup>.

The lack of taxation results in special informative duties. These special requirements are so far described in the part I of this thesis.

When it comes to estate tax, the Law on taxes and local levies has to be analyzed. Each non-profit organization needs any place to run its activity. In this way real estate tax comes into consideration. Both subjective and objective scope of the Law on taxes and local levies does not exclude non-

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<sup>41</sup> The individual interpretation of the Minister of from 8<sup>th</sup> December 2008 (IBPB2/436-155/08/MCZ).

profit organizations. Pursuant to objective scope of this Act, all estates (ground and buildings) are taxed. Special exclusions are provided mainly for public purposes (e.g. ground for public roads or seats of authorities). In the Law on taxes and local levies there are only three exemptions which are connected with non-profit activity.

Pursuant to the provision art. 7 para. 1 point 5 of the Law on taxes and local levies, estates or their parts are tax exempted, if they are used by associations for their statutory purposes of sport or education activity among children and teenagers. Tax exempted are also grounds which are constantly used for organizing camps for children and teenagers. The exception of this exemption are estates used to run business. A subject of this regulation may be only these non-profit organizations which act in the legal form of association. The status of public benefit organizations is not required.

Another tax exemption which is relevant for non-profit activity is stipulated in the provision art. 7 para. 1 point 14 of the Law on taxes and local levies. Pursuant to it, tax exempted are estates where public benefit organizations run their statutory gratuitous activity. This exemption requires possessing the status of public benefit organization. It means that not every non-profit organization may benefit from the exemption.

The last special regulation provided for non-profit organizations refers to maximal tax rate of estate tax which local authorities may declare. There is stipulated special maximal tax rate for chargeable activity of public benefit organizations which is lower than for normal business activity but higher than for housing purposes.

The analysis of provisions of the Law on taxes and local levies lead to conclusion that the status of public benefit organization allows the greater number of tax benefits. Without this special status, there is only the part of non-profit activity which does not pay estate tax. This group of organization is limited both by the purpose and the legal form of activity. In this way legislator favours public benefit organizations in comparison to non-profit activity without this status.

This distinction does not exist on the ground of the Inheritance and gift Act. The Act do not provide for taxation of donations and inheritance acquired by any kind of legal person. As in Poland all legal forms of non-profit organizations may be established only as legal persons, it is obvious, that any kind of discrimination of some of non-profit organizations does not exist. As the result of this regulation there is lack

of taxation also in case when one non-profit organization make a will or donation to other domestic non-profit organization. Although there are no special provisions, it is obvious that also when a foreign non-profit organization makes a will or donations to a domestic non-profit organizations, this actions is not taxed on the ground of Polish legislation. In the opposite direction, tax consequences depend on foreign tax jurisdiction and its regulation.

## 5. Other taxes

Each non-profit organization undertakes many different actions during its existence. The first step of founders of any organization is to register it. Later, a non-profit organizations conclude contracts which are necessary to run their activity. These all actions are taxed. The question is then, if there are provided for some special provisions for non-profit organizations.

During registration each organization is obliged to bear certain costs. Basic fee is a registry fee for registration in National Court Register (where all legal persons are to be registered). It is associations and public benefit organizations that are exempted from this fee. Other non-profit has to bear this cost unless they move for exemption. Such an organization has to prove that it is not able to bear this cost<sup>42</sup>. Another possibility to be exempted from a registry fee is pointing that an organization is not going to run business activity but run social, education, sport or charitable activity<sup>43</sup>. Both exemption are however a result of granting a petition. In order to be exempted, an organization has to file a petition. The only fee which an organization cannot be exempted from is fee for entry in the Court and Commercial Magazine. However, the entry in the Court and Commercial Magazine is required only then when an organization is going to run business activity.

Special treatment is provided for public benefit organization. They are exempted from register fee in advance. Acts undertaken within business activity are the only exception. This sphere of activity is required to be registered as normal business activity. It means that in reference to this activity there has to be paid registry fee. Tax exempted are also associations as well as foundation if they perform any act as commissioned tasks on the ground of the Public Benefit Act. The difference between this exemption and the first one is that public benefit organization and other organizations which perform their tasks do not have file a petition to the court. The exemption is granted *ipso iure*.

Another very important levy which might stand for another fiscal burden for non-profit activity is civil act tax. The subjects of taxation are different civil acts which are enumerated in the Law on civil acts tax. Among them are listed: the contract of sale, exchange of goods or rights or a loan. These actions are the most often undertaken acts by non-profit

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<sup>42</sup> The art. 103 of Court fee act (Dz.U. 2010 Nr 90, poz. 59, herein: the Court fee act).

<sup>43</sup> The art. 104 para. 2 of the Court fee act.

organizations. However, there is provided special tax treatment in the Act for public benefit organizations. Pursuant to the art. 8 point 2a of the Law on civil acts tax public benefit organizations are tax exempted, if they perform any civil act in reference to gratuitous public benefit activity<sup>44</sup>. It means that non-profit organization which do not have the status of public benefit organization cannot benefit from special tax treatment provided in this Act. Even public benefit organizations are not allowed to be exempted, if the subject of their act is not free of charge.

If a non-profit organization which do not have a status of public benefit organization concludes a contract of a loan, it is not certain that it is going to pay tax. In case of a loan, the legislator prepared exemption which depends on the amount of money which is granted to a non-profit organizations. A contract of a loan which is concluded between organizations or organization and other person (natural or legal) is also tax exempted, if the value of borrowed goods or rights is not higher than 4 902 PLN (circa 1300 EURO).

During its existence non-profit organization not only conclude civil contracts. It sometimes has to perform some actions in front of public administration. In Polish jurisdiction some of these acts are subject to stamp tax. The simplest example is a proxy. In order to make a proxy effective, any entity has to pay stamp tax. Similar as it is on the ground of the Law on civil acts tax, special tax treatment is provided only for public benefit organizations. The exemptions refers to all actions which are in reference with gratuitous public benefit activity.

As may be noticed after this short analysis, the special activity and role in the society of non-profit organizations is noticed by the legislator. Nevertheless, the most of tax benefits are granted only to these which have the statue of public benefit organization. However, their activity is better controlled under the Public benefit act. There are more requirements which are to be met in order to become a public benefit organization. They have to meet more conditions than typical associations or foundations. Maybe it is the reason for wider scope of benefits.

In the conclusion it has to be underlined that other levies as e.g. vehicle tax do not provide for any special provisions exempting from tax burden or lowering it. Only those strictly connected with non-profit activity envisage the role of non-profit organizations.

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<sup>44</sup> Public benefit activity is understood the same as in the Public benefit Act.

## Summary and conclusions

In the Polish legal system there are provided for provisions which allow running non-profit activity. Civil law and special entities which it forms (as for instance foundation or associations) are not enough to enhance the third sector. Each charity exists as a part of economy. It has to carry the same burdens as other participants of the market. Taking into account the special role which the third sector plays in the society, it seems to be adequate to encourage their development. The legislator is the only one who possesses proper measures. What the legislator can do is decreasing burdens which non-profit organization normally would have to bear.

Taxation is the area of law which participant of the society takes into account. Although we may claim that the system of taxation should be neutral and should not influence economic decisions, it is impossible to avoid it. A legislator know that. Therefore, in many tax systems they provide for special tax instrument for non-profit organizations.

In Polish tax law there are special preferential tax rules for non-profit activities. However, no tax acts does recognize the term of non-profit activities or non-profit organizations. Preferential rules refer to the purpose of entities which are created by the civil law (e.g. foundation, association). There is only one entity which is granted tax benefits regardless of its purpose. It is a public benefit organization. The legislator expressly favours this form of activity. On the ground of different tax acts (income tax acts, the VAT Act or the Law on civil acts tax) public benefit organizations are treated the most favourable.

There may be noticed general tendency of the legislator to exempt those kinds of income which are appropriated on purposes which are socially acclaimed. In both cases: exempted entities because of the purpose of their activity or those that possesses the status of a public benefit organization there is no disparity in the tax treatment of income coming from non-profit activity, from business or investment. There is only one exception from this rule. The general conclusion may be: the prerequisite of tax exemption on the ground of income taxes is the purpose of appropriation.

Nevertheless, the preferential treatment of non-profit organizations does not refer to remuneration of employees or administrators of non-profit organizations. Non-profit organizations are obliged to follow the same duties as other employers, because the income of its employers is taxed without any preferential or at least special rules.

In order to enhance the development of the third sector special tax treatment of non-profit organizations is not enough. It is important to take into account the role of donors who contribute the activity of non-profit organizations. In this scope Polish legislator prepared special deductions from income and from tax. These refer only to public benefit organizations. In this way it is advantageous for taxpayers to donate this special form of activity.

Special tax treatment of the third sector is not only a feature of income tax acts. Particular provisions are found on the ground of VAT Act as well. Generally, non-profit organization may be tax exempted, if their services are compliant with purposes pointed in the VAT Act. It is a public benefit organization again which is treated on the ground of VAT Act more favourably.

The Polish legislator takes into account not only Polish non-profit organizations. Most of cases analyzed in the thesis provide for preferential tax treatment of not only Polish third sector. In the income tax acts exemptions directed to public benefit organizations refer also to foreign institutions which are granted similar character. Nevertheless, this equal treatment of Polish and foreign organizations is pointed not in all tax acts. There is lack of such a special provision e.g. in the Law on civil acts tax. Even under provision of income tax acts (PIT Act or CIT Act) there arises always the question whether there are not too many obligations to be met in order to benefit from tax equal treatment. Especially, the provision referring to holding a company by an association may be deemed as discriminative. The wording of this provision brings to mind reflection whether foreign associations are allowed to benefit from it. It seems that they are not. There is no clear answer since it is hard to find any evidence in the tax practice.

The analysis of Polish tax system from the point of tax treatment of non-profit activity proves that the legislator notices the special role of the third sector. As a conclusion it has to be noticed that a legal person acting as a non-profit organization is granted a special tax treatment. In the same time a natural person which receives the aid of such an organization is obliged to pay tax. The lack of exemption in this case surprises. The question which may be posed is whether the legislator truly encourages to support activity of the third sector.

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