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## New rules for documenting transactions with tax havens - are you prepared?

From the beginning of 2021, transfer pricing documentation (Local file) is prepared for transactions with related entities and settlements made directly with entities from a tax haven and **for a number of transactions with unrelated entities**. Preparing documentation for 2021, taxpayers will have to prove to the authorities their use. The change is particularly important if you have not yet made settlements with related entities and had no interface with the provisions on transfer pricing.

### 1. NEW DOCUMENTATION OBLIGATIONS

From 1<sup>st</sup> of January 2021, the transfer pricing regulations addressing tax haven transactions have been significantly expanded.

For transactions made with entities from tax havens, the documentation obligation covers:

- 1) **transactions other than the controlled ones** (other than transactions with related parties) made with an entity having place of residence, registered office or management board in the territory or in a country applying harmful tax competition, if the value of the transaction for the tax year (and for the financial year in the case of companies without legal personality), **exceeds PLN 100,000 net** (about EUR 25,000 net);
- 2) **controlled transactions or non-controlled transactions if the beneficial owner<sup>1</sup>** has a place of residence, registered office, or management in the so-called **tax haven**, and the value of such a transaction in the financial year **exceeds PLN 500,000 net** (approximately EUR 110,000 net). The legislator presumes that the actual owner has a place of residence, seat, or management in the so-called tax haven whenever the contractor of a taxpayer or a company without legal personality makes settlements in the tax year with an entity having its registered office or management in the so-called tax haven.

Therefore, starting 2021, documentation obligations in the field of transfer pricing may be in place not only for direct settlements with an entity (related or unrelated) having a place of residence, registered office, or management in the territory of a country applying harmful tax competition. They may also apply to a transaction made with an entity (related or unrelated) whose beneficial owner is an entity from the so-called tax haven.

<sup>1</sup> According to the definition of the beneficial owner indicated in article 4a point 29) of the CIT Act (hereinafter: '**beneficial owner**').

This basically means that if the beneficial owner of the contractor (even an unrelated one) is an entity from a tax haven, then the transfer pricing regulations apply. This also triggers the need to meet certain obligations. An additional difficulty is that the taxpayer must verify its contractors in terms of their transactions with entities from tax havens. If the taxpayer is unable to confirm whether its contractor does not make transactions with entities from tax havens, then it is presumed that the beneficial owner of this contractor is an entity from the tax haven. And this is equivalent to the need to comply with tax obligations.

## 2. EXTENDED DOCUMENTATION REQUIREMENTS

Entities that have identified documentation obligations as a rule must:

- prepare **local transfer pricing documentation (the so-called Local File)** for the transaction for which the documentation was required. The documentation for "tax haven transaction" must additionally contain an economic justification, in particular a description of the expected economic benefits, including tax benefits (benefit test),
- submit to the tax authority a **TP Statement** signed by the management board, **confirming the preparation of local transfer pricing documentation** for transactions with related entities, as well as tax havens transactions, along with a **declaration of the arm's length nature of the prices applied**,
- file **Information on Transfer Prices (the so-called TPR form)** - it summarizes the general financial situation of the taxpayer and the controlled and tax havens transactions it made.

A favourable change for the taxpayers is the proposed simplification under the so-called "Polski Ład" to apply retroactively, i.e. from 1<sup>st</sup> of January 2021. These changes will include removed obligation to prepare transfer pricing analyzes (analyzes justifying arm's length character of transaction) in the case of tax haven transactions made with unrelated entities. At the same time, taxpayers must be still verifying the beneficial owners and subject to reporting obligations (transfer pricing documentation, TPR).

## 3. ACTIONS TO BE TAKEN BY THE TAXPAYER

The implemented changes may become a significant challenge in terms verifying contractors as well as preparing documentation.

**It is the right time now to see how to exercise due diligence in verifying contractors in terms of documentation obligations in transfer prices to avoid disturbing regular operations and business relations.**

To exercise due diligence, taxpayers must prepare and collect statements regarding transactions made by their contractors with tax havens. In addition, it is worth implementing additional solutions across the organization, i.e. dedicated provisions in contracts with contractors, as well as drawing up and implementing a detailed contractor verification procedure.

It is worth acting now because the deadline for preparing documentation for 2021, including tax haven transactions, is the end of October 2022.

The deadlines may seem distant yet given the complex and lengthy procedure of obtaining statements from contractors, it is worth establishing the contractor verification process before the end of the year.

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#### 4. TAX HAVENS

The Regulation of the Minister of Finance of 28<sup>th</sup> of March 2019 on the determination of countries and territories applying harmful tax competition in the field of corporate income tax lists 26 countries (territories) whose tax systems feature harmful tax competition. Among them are: Principality of Andorra, Anguilla - Overseas Territory of the United Kingdom of Great Britain and Northern Ireland, Antigua and Barbuda, Sint-Maarten, Curaçao - countries included in the Kingdom of the Netherlands, Kingdom of Bahrain, British Virgin Islands - Overseas Territory of the United Kingdom of Great Britain and Northern Ireland, Islands Cook - Self-Governing Territory Associated with New Zealand, Dominica, Grenada, Sark - Dependent Territory of the British Crown, Hong Kong - Special Administrative Region of the People's Republic of China, Republic of Liberia, Macau - Special Administrative Region of the People's Republic of China, Republic of Maldives, Republic of Marshall Islands, Republic of Mauritius, Principality of Monaco, Republic of Nauru, Niue - Self-Governing Territory Associated with New Zealand, Republic of Panama, Independent State of Samoa, Republic of Seychelles, Saint Lucia, Kingdom of Tonga, Virgin Islands - United States Unincorporated Territory, Republic of Vanuatu.

In addition, the list of "tax havens" has been completed in accordance with the Notice of the Minister of Finance of 7<sup>th</sup> of July 2020, containing the list of countries and territories indicated in the EU list of non-cooperative jurisdictions for tax purposes adopted by the Council of the European Union. It includes Republic of Fiji, Guam, Cayman Islands, Republic of Palau, Sultanate of Oman, Republic of Trinidad and Tobago, American Samoa.

Interestingly, the reported transactions with tax havens for 2019 totaled PLN 140,218.02 million - most of them with Panama and Hong Kong (86.27% of total tax havens transactions).

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