

LIMITED PARTNERSHIPS – NEW CIT TAXABLE PERSONS?

On 16 September 2020, on the portal of the Government Legislative Centre (rcl.gov.pl), the government's draft amendment to several pieces of tax legislation was published, including primarily the Personal Income Tax Act (the PIT Act) and the Corporate Income Tax Act (the CIT Act). Among the changes planned to take effect from the beginning of 2021, each of which deserves a separate discussion, the most important one seems to be the **change in the status of limited partnerships** (LPs) (Polish: *spółki komandytowe*) **and some registered partnerships** (RPs) (Polish: *spółki jawne*).

It is well-known that both the LPs and the RPs are currently the so-called fiscally-transparent entities. This means that income tax on the income earned by such partnerships is accounted for by their partners, according to their share of profit. Those partners who are natural persons are liable for personal income tax (PIT), and the legal persons who are partners in such partnerships are liable for corporate income tax (CIT).

According to the Government's plans, starting from 1 January 2021, **all Polish**



limited partnerships are to become CIT taxable persons. These plans also apply to **general partnerships with their registered office in Poland where the partners are not only natural persons, if they do not submit the relevant information about their partners**

(draft Article 1(3)(1a) of the CIT Act).

This is not the first attempt at making partnerships CIT taxable persons. Since 2014, limited joint-stock partnerships (Polish: *spółki komandytowo-akcyjne*) have become CIT taxable persons. The current draft is introduced under the same catchphrase as the one used seven years ago: limitation of aggressive tax optimization. Such a justification of the proposed changes is questionable if we take into account the scale of the phenomenon of aggressive tax optimization with the use of limited partnerships, as compared to the use of this legal form without the intention to avoid tax, in “ordinary” activities, especially in the sector of small and medium-sized enterprises.



In any case, the mechanism of taxation in limited partnerships is based on the same assumption as that underlying the taxation of limited joint-stock partnerships. The point is that the partners who have unlimited liability for the entity’s obligations (general partners) should not be burdened with additional levies, whereas those who are not generally liable for the entity’s obligations (limited partners) should be treated in the same way as shareholders of limited companies, whether private (*Sp. z o.o.*) or public (*S.A.*).

The objectives are to be achieved in three stages:

- the limited partnership will account for CIT on its current income on the same terms as limited companies and limited joint-stock partnerships, and at the same rates, i.e. 19% or 9% – for those entities whose annual revenue does not exceed EUR 2 million (the same amendment provides for an increase of the current limit of EUR 1.2 million to this amount);
- the limited partnership’s payment of profit to its partners will be treated just like distribution of dividends by a limited company (share in the profits of legal persons), i.e. it will be subject to taxation at a fixed rate of 19%, regardless of whether the partner is a natural person or a legal person;
- the effect of “double taxation”, which will arise after the distribution of profit by the limited partnership, will be eliminated as the general partners will be granted the right to reduce the tax due on the distributed profit share by an

amount corresponding to: the general partner's percentage share in the partnership's profits multiplied by the tax due on the partnership's income for the year for which the profit was distributed. Only general partners will have this right, whereas the income attributable to limited partners is, by definition, subject to "double" taxation.

Profit distribution is usually made in the year following the year for which the profit was earned. However, if the limited partnership does not pay out the profit at that time, the right to reduce tax can also be exercised if the profit is distributed later, but not longer than for five consecutive tax years, counting from the end of the tax year following the year in which the profit was earned. This rule has been in force since 2014 in relation to general partners of limited joint-stock partnerships.

Although in principle limited partners are to be subject to "double" taxation, they should at the same time be treated just like shareholders of limited companies. This means, among others, that they will be fully exempt from the tax on "dividends" (share in profit) distributed by the limited partnership under the conditions set out in Article 22(4) of the CIT Act. This exemption is granted to entities that have their registered office in any EU country, EEA country or Switzerland and have had a minimum holding of 10% (in the case of Switzerland – 25%) in the capital of an entity distributing the profit (for a limited partnership, this will be 10% and 25%, respectively, of the value of contributions to that partnership) for at least 2 years.

All limited partners who do not meet the above condition, whether legal persons or natural persons, will be entitled to an exemption in respect of the amount equal to 50% of revenue generated from participation in the limited partnership, but not more than PLN 60 thousand. This limit, if a given entity is a limited partner in many partnerships, applies to each partnership separately.

We will be keeping a close eye on this draft amendment. According to the principle developed many years ago by the Constitutional Tribunal, any amendments to PIT and CIT should be published in the Journal of Laws on 30 November at the latest.

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