

Setting up a Limited Liability Company in Poland

December 2008

General
<p>The Commercial Companies Code (KSH) regulates all issues related to the establishment, activity and dissolution of these companies. The existing legal framework allows companies ample flexibility in drawing up their company deeds. Certain regulations of the Commercial Companies Code are not obligatory and can be modified by the incorporation documents. The company deed, as well as all subsequent changes, must be prepared in the form of a notarial deed, and are otherwise null and void.</p>
Establishing a Company
<p>Establishing a company with foreign participation in general does not require the prior obtaining of a permit or license.</p> <p>One or more legal or natural persons may establish a limited liability company but a one-person limited liability company may not incorporate one.</p> <p>A company deed or statute must define the following:</p> <ul style="list-style-type: none"> • name, place of incorporation and scope of activities of the company; • duration of its activity - if it is to be established for a definite period; • value of share capital;; • the company deed for limited liability companies must state whether a shareholder may have one or more shares and what are the numbers and value of shares held by respective shareholders; • the form in which initial capital will be contributed and the number and value of shares issued where equity is contributed in kind; <p>In order to obtain legal status and to be able to commence activities, a company must:</p> <ul style="list-style-type: none"> • appoint members of its managing and supervisory bodies; • be recorded in the National Business Register in the relevant District Court. <p>Registration is possible only after the entire equity capital has been paid in and after the transfer of the in-kind contributions has been guaranteed.</p>
Share Capital
<p>In limited liability companies, the minimum amount of initial share capital up to 7 January 2009 is PLN 50,000 divisible into shares of equal or unequal value. Following a new law, as from 8 January 2009, the minimum amount of share capital to set up a limited liability company becomes PLN 5,000.</p> <p>The lowest permitted value of a share is PLN 50. If the company deed allows one of the shareholders to hold more than one share, then all shares must be equal in value and indivisible.</p>
Increase and Decrease in Share Capital
<p>In limited liability companies, changing the nominal value of existing shares or issuing new ones may</p>

increase the share capital. If the company deed provides for equity increases, then such increases require only a majority vote of the shareholders.

If not, then the company deed itself has to be amended, for which the consent of two-thirds of the shareholders is necessary, unless the company deed provides more stringent voting requirements.

A decrease in capital is possible only through a vote of the shareholders, which must also specify the amount and form of the decrease. However, the decreased capital may not be lower than the minimum equity prescribed by law, i.e. PLN 5,000

Current shareholders in a limited liability company have priority in taking up the increased shares in proportion to the shares already held, unless the pre-emptive right is restricted or excluded by the company deed, statute or a resolution of the shareholders.

Capital decreases may not be made to the detriment of the interests of creditors, thus a company's management board is required to notify all affected parties. Affected creditors must be satisfied or their interests otherwise secured.

Profits are distributed to shareholders, unless the distribution has been restricted in the company deed. Profits are distributed in proportion to the shares, unless otherwise provided in the company deed. Shareholders can cover losses, until the loss exceeds the aggregate reserve capital and half of the share capital. In such an event, shareholders have to vote whether or not the company should be dissolved.

Additional Payments to Share Capital

Additional payments are made by shareholders to finance working capital requirements. They can be made in addition to the shareholders' loans and they have no effect on the amount of equity, or the value of shares held by the shareholders.

The possibility of making additional payments arises solely from a specific regulation placed in the company deed, indicating the value of the additional payment proportionally to the held shares. If the deed does not provide for such an obligation, additional payments can only take place after the company deed has been amended. Decisions as to the amounts and dates on which the payments are to take place are left to the shareholders' discretion. If the paid-in amounts are not necessary in order to cover losses, they may be transferred back to the shareholders.

The Management Board

The company's managing body is the management board, consisting of one or more members who are usually appointed by the shareholders. Members of the management board may be appointed from among the shareholders or other persons, irrespective of whether they are Polish nationals or foreigners.

If it has more than one member and the company deed or statute does not provide otherwise, in its dealings with third parties a company must be represented by two members of the board, or one member and a proxy acting jointly.

A member of the management board cannot, without the consent of the company, engage in competitive activities, be a member of the managing or supervisory bodies of a competitor company or be a partner in a partnership which is a competitor.

Supervisory Bodies

The company deed of a limited liability company may provide for the appointment of a supervisory board or an audit commission, or both. In companies with share capital in excess of PLN 500,000 and more than 25 shareholders, one of these two bodies is obligatory. Each body must have at least three members.

A member of the current management board, the company's liquidator and certain senior employees (e.g. chief accountant, legal counsel, etc.) may not be members of either of the company's supervisory bodies.

Shareholders' Meetings

The shareholders' meeting is the decision-making body in matters of major significance to the company. Its meetings may be ordinary or extraordinary.

An ordinary general meeting should take place once a year. It should be held during the first six months of the financial year.

Extraordinary general meetings may be convened at any time or when required by law. The annual general meeting examines and approves reports from the supervisory and management bodies and the financial statements, and discharges the management board and the supervisory board with regard to the performance of their duties during the preceding financial year. It decides on the payment of dividends or coverage of losses if the deed expressly provides for such a possibility).

The annual general meeting rules, inter alia, on the following matters:

- ways of covering losses incurred during the establishment of the company, its management or supervision
- transfer or lease of the company's business and charges in rem (e.g. pledge) on this business
- reimbursement of supplementary payments
- increase or decrease of equity
- changes in the company's scope of activities
- dissolution of the company

During the first two years after registration of a limited liability company, a shareholder's resolution is necessary to approve the purchase of real estate or fixed assets with a cost in excess of PLN 50,000 if this exceeds one fourth of the share capital.

Ordinary and extraordinary general meetings are convened by the management board and can only be held in Poland. Shareholders representing at least 1/10 of the capital may demand that the management board convene an extraordinary meeting. In the event that the management board fails to do so within two weeks, shareholders are entitled to convene an extraordinary meeting after they receive authorization from the Registry Court.

Shareholders can participate in meetings either in person or through representatives. The company deed of a limited liability company may provide restrictions in this respect.

For a power of attorney to be valid, it must be made in writing and attached to the formal minutes of the meeting. Decisions of the meetings of the general assembly are generally passed by a simple majority of votes cast. Qualified majority votes are needed only in specific situations. Whenever these changes increase ownership commitments or restrictions of their rights, all affected shareholders must consent.

Dissolution and Liquidation

A company is dissolved if, inter alia, the following situations arise:

- circumstances anticipated in the company deed or statute occur, i.e., when the company reaches the end of the period for which it was set up
- shareholders decide on the dissolution of the company (with regard to the obligation to convene extraordinary shareholder's meeting due to significant losses, or to decide on the further operation of the company)
- shareholders decide to move the registered office or principal activity abroad
- a court so decides that the aim for which the company has been established cannot be reached, or another important change in the company's internal situation occurs
- a court so decides upon the request of the General Prosecutor in the event that the company breaches the law and its further existence is contrary to the interests of national security

The commencement of the liquidation procedure must be registered in the registration court and announced in the Official Polish Legal Journal, together with a notification to creditors to submit their claims (they must do so within three months after the public announcement).

Shareholders may distribute the remaining assets in proportion to their participation in ownership only after the company has settled or safeguarded the interests of creditors. This distribution can occur only after a period of six months from the date of the liquidation announcement and the announcement to creditors has lapsed.

Once the liquidation is terminated, the liquidator is authorized to prepare a final liquidation report and file it with the National Business Register with a request to strike off the company from the register.

Taxation Issues

Polish taxation is not straightforward and experts' advice should always be sought.

Taxation of rental income

Net rental income received by corporate owners (irrespective of whether they are Polish or foreign companies) is taxed at the standard corporate income tax rate of 19%. Generally expenses incurred by owners while earning this rental income, including interest paid on loans used to acquire the property,, are deductible for corporate income tax purposes, unless they fall within those categories of expenses which the legislation states are not tax deductible. Expenses must be properly documented in order to be tax deductible.

Thin capitalisation

The legislation sets out a minimum debt-to-equity ratio of 3:1 for loans drawn down from qualifying lenders (including shareholders owning at least 25% of shares in the borrower as well as from "sister companies" if the same shareholder holds at least 25% of shares in both the lender and the borrower.

When this ratio is exceeded, interest paid on restricted loans, in relation to the part of the loans exceeding three times the value of the borrower's share capital will not be tax deductible.

Depreciation

Accounting depreciation procedures are similar to those in Cyprus. Although depreciation for tax

purposes is normally based on accounting depreciation, it is possible to have differences between them.

Taxpayers can you two basic methods of depreciation – straight line and reducing balance. Tax deductible depreciation is subject to maximum straight line rates. For buildings, depending on type, these rates range from 1.5% to 10% annually. Usually non-residential buildings are depreciated over 40 years, using a 2.5% annual depreciation rate.

Polish law provides for accelerated depreciation for assets used in conditions of intensive use. The definition of intensive use is use more intensive than in average conditions or subject to exceptional technical demands.

Land is not depreciated for tax purposes.

Loss carry forward

Losses may be carried forward for five consecutive tax years with no more than 50% of amount of the loss from each year to be utilised in any one year.

Withholding tax

The standard rate of withholding tax on dividends is 19%. This is reduced to 10% under the Cyprus-Poland Double Taxation Avoidance Agreement. This applies equally to the distribution of liquidation proceeds and the issue of new shares from retained earnings.

However under the EU Parent Subsidiary Directive no withholding tax needs to be withheld if all of the following conditions are met:

The Cypriot recipient owns at least 15% of the share capital of the Polish company.

The shares have been owned or will be owned for a continuous period of 24 months

The Cypriot company is resident for tax in Cyprus

From 1 January, 2009 the qualifying percentage will be reduced to 10%.

Interest and royalty payments are subject to a standard withholding tax rate of 20%. This is reduced to 5% under the Cyprus-Poland Double Taxation Avoidance Agreement. This is more favourable than the interim rules in place under the EU Directive on Withholding Tax on Interest and Royalties, which is 10% until 30 June 2008. From 1 July 2009 it will be 5%

Intangible services rendered by a foreign company to a Polish company are subject to a standard withholding tax rate of 20%. However this is reduced to zero under the Cyprus-Poland Double Taxation Avoidance Agreement.

Transfer Pricing

Polish transfer-pricing rules are—in principle—based on the OECD transfer-pricing guidelines. The rules are based on the concept of the arm's-length level of transfer prices. If related entities (eg with a common shareholder) conclude transactions on terms that differ from market practice and as a result the Polish entity discloses taxable income lower than it would otherwise disclose, the taxable income of the entity will be adjusted on this principle.

Moreover, if intangibles or services are the subject of such a transaction, and the benefits rationally expected from the transaction are obviously lower than the expenses incurred, then such expenses are not deductible for tax purposes.

With regard to selection of transfer-pricing methods, the Polish tax authorities show strong preferences for the use of the comparable uncontrolled price method (CUP). Taxpayers who use other methods to price their intercompany transactions are expected to defend their selection.

Adequate records should be kept to prevent the tax authorities from application of simplified CUP methodology and defend returns consistent with the risk/reward profile of the Polish company.

The scope of the documentation requirements basically follows the OECD documentation standards.

Taxpayers must present the documentation in Polish within seven days of the request of the tax authorities. If the authorities determine that the taxpayer's profit is higher (or the loss is lower) than the amount declared by the taxpayer, and the taxpayer does not provide the authorities with the documentation required, the difference between the profit declared by the taxpayer and the profit determined by the authorities may be subject to tax at 50%.

Changes in transfer-pricing regulations, allowing taxpayers to apply for advanced pricing agreements (APAs) with the tax authorities, were introduced on 1 January 2006.

Pursuant to the new regulations, taxpayers may apply for a domestic and international uni- and bilateral APA. The APA will be issued for a period of three years, with the possibility of extension for the following three years.

Capital gains

Poland has no distinct capital gains tax. Gains are subject to the standard rate of corporate income tax, currently 19%.

Some double taxation avoidance agreements including the Cyprus-Poland Double Taxation Avoidance Agreement, exempt the capital gain arising from the sale of Polish real estate holding companies from Polish taxation. However, the direct sale of Polish real estate by a foreign company is subject to Polish taxation.

VAT

The sale of land and buildings is generally subject to VAT at the standard rate of 22% recoverable under standard VAT rules. VAT is also due on all net pre-payments. Under some conditions sale of second-hand land and buildings may be exempt from VAT – but in this case 2% Civil Law Activities Tax would apply. Buildings are regarded as second-hand if they were used by the previous owner for a minimum of 60 months before the acquisition. Such classification of the building influences the transfer tax treatment of the land on which the building is located.

The above standard VAT is reduced to 7% with respect to the original (first after finishing the construction) disposal of residential buildings until 31 December 2007. The subsequent transfer of residential buildings are VAT exempt.

VAT at the rate of 22% is also generally applicable to income from the lease of buildings, except for residential buildings, leasing of which is VAT exempt under certain conditions. This is generally recoverable by the tenants as input VAT. However, companies providing exempt services (e.g. financial services) are generally unable to recover input VAT. Charges for the lease or rental of property situated in Poland are subject to Polish VAT, even if the charge is made to a non-resident foreign company.

NOTES:

The above is intended to provide a brief guide only. It is essential that appropriate professional advice is obtained. Totalserve Management Ltd will be glad to assist you in this respect. Please do not hesitate to contact us.