

## **PROFESSIONAL TRADE IN PROPERTY**

Polish law regulates professional trade in property principally as an economic activity conducted with the aim to obtain commercial gains. Consequently, only entities that belong to the so-called professional category, that is entities conducting registered economic activity, are required to pay taxes on professional trade in property. Under Art. 2 of the Act of 2 July 2004 on freedom of economic activity<sup>1</sup>, economic activity is defined as commercial activity consisting in manufacturing, construction, trade, services, exploration and mining of minerals from deposits, as well as professional activity conducted in an organized and continuous fashion. However, for tax purposes, this definition is inadequate. In the area of taxation of professional activities, the tax law introduced detailed definitions of economic activity that are different from the one presented above. Taxation of professional trade in property is regulated by three tax laws: the act on personal income tax, the act on corporate income tax, and the act on value added tax. The latter act, by introducing the broadest definition of economic activity, has brought about a number of problems of interpretation.

Art. 5a item 6 of the Act of 26 July 1991 on personal income tax<sup>2</sup> defines economic activity as commercial activity consisting in manufacturing, trade, services, exploration or mining of minerals from deposits, as well as activity consisting in using objects or intangible and legal values, conducted on one's own behalf, regardless of its result, in an organized and continuous fashion. Thus, the definition of economic activity for the purpose of personal income tax is a little broader than the definition provided in the act on freedom of economic activity. According to Art. 9 passage 1 of the act on personal income tax, all sorts of income are subject to taxation. On the other hand, Art. 10 passage 1 item 4 of the act defines sources of revenue as real estate or its parts, as well as paid transfer of ownership of real estate or its parts, or co-ownership of real estate (Art. 10 passage 1 item 8 letter a of the act). This leads to the conclusion that professional trade in property is subject to personal income tax under the condition that it takes the form of an economic activity conducted by

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1 i.e. Journal of Laws No. 55 (2007), item 1095 with changes.

2 i.e. Journal of Laws No. 14 (2000), item 176 with changes.

entrepreneurs. Depending on the taxpayer's choice of the personal income tax, the income earned by the entrepreneur can be subject to the regular tax rates (19%, 30%, or 40%), or to a flat tax (19%). It is the taxpayers who make the choice. Nevertheless, to be eligible for the flat tax, the taxpayer must submit to his local branch of the tax authorities a declaration on the selected form of taxation.

A similar structure of professional trade in property is incorporated into the Act of 15 February 1992 on corporate income tax<sup>3</sup>. The taxpayers who are covered by the provisions of this act are legal persons and entities who do not have the status of legal persons with respect to income from professional trade in property. The tax rate for such entities is equal to 19%. Of course, for the purpose of both personal income tax and corporate income tax, expenses related to the acquisition of property to be sold later constitute costs that can be deducted from the revenue, with the exception of trade in property conducted by such entities as real estate brokerages where it is the commission of these entities that is subject to taxation.

The law on value added tax provides for different solutions concerning professional trade in property. This results from the fact that the Act of 11 March 2004 on value added tax<sup>4</sup> does not require taxpayers to conduct a registered economic activity to be subject to this tax. This provision causes a number of controversial interpretations with regards to the question whether a natural person who delivers (sells) real estate is subject to this tax. In order to correctly present the issue of taxation of professional trade in property, one has to start with the basic definitions related to this tax, which are different from those presented above. According to Art. 15 of the Act on value added tax, the taxpayers of this tax include natural persons who conduct individual economic activity, regardless of its goal or outcome. In passage 2 of this provision, the legislator introduces a definition of economic activity as an activity that encompasses all types of work conducted by manufacturers, traders, or service providers, even when this activity is performed a single time in circumstances indicating that it is intended to be conducted frequently. This regulation explicitly stipulates a list of entities that are subject to this tax. The list includes manufacturers, traders, and service providers, that is "professional" entities or entities that conduct economic activity. What this means is that the very definition of "a taxpayer" excludes applying the provisions of this act to natural persons who do not conduct registered economic activity. However, this understanding is not so clear in the interpretations of Polish tax authorities. The definition of "a taxpayer" is essential to the determination of the scope of taxation since only activities that meet the subjective and objective criteria are subject to this tax. What this means is that a taxable activity must be performed by a subject who meets certain criteria

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3 i.e. Journal of Laws No. 54 (2000), item 654 with changes.

4 Journal of Laws No. 54 (2004), item 535 with changes.

to be considered a taxpayer. Both of these conditions must be met simultaneously and, therefore, the subject must meet the criteria of a taxpayer in any given activity. Consequently, if a taxable activity is performed by a subject who does not meet the criteria of a VAT taxpayer, in principle, it is not taxable. The provisions of the 6<sup>th</sup> directive (similarly to those of the 2006 directive no. 112/2006/WE on the VAT) explicitly list this requirement as they regulate the performance of taxable activities by a taxpayer acting in such a role<sup>5</sup>.

A similar opinion is presented in the judicial decisions of Polish provincial courts of administration. In its decision of 6 September 2006 (sign. of the record I SA/Wr 1254/06), a provincial administrative court declared that the sale, even repeated, of privately owned objects which are not related to economic activity and had not been purchased for the purpose of re-sale, does not meet the criteria of trade and, therefore, is not subject to the VAT tax. In its decision, the court also stated that “the fact that the subject is performing activities stipulated in Art. 5 of the Act on the VAT tax does not constitute a sufficient premise to consider these activities as covered by the requirement to pay the VAT tax because the activities must be performed by a subject who is a taxpayer in the understanding of this act, i.e. a subject conducting an individual registered economic activity.” A similar opinion was presented by the Supreme Court of Administration in its decision of 24 April 2007 (sign. of the record I FSK 603/06) where it stated that trade should be defined as an organized purchasing of goods with the aim of their re-sale and that the condition for considering a given person as a taxpayer is the person’s constant involvement in the conduct of an economic activity. The court provided a profound justification and a comprehensive explanation of who can be regarded as a taxpayer of the VAT tax. According to the Court, in order for a given activity to be subject to the value added tax, the following two premises must be fulfilled simultaneously:

- first: a given activity must be included in the list of activities that are subject to the value added tax,
- second: the activity must be conducted by a subject who is a VAT taxpayer in relation to the performance of this activity.

Moreover, the Court concluded that trade should be defined as an organized purchasing of goods with the aim of their re-sale. Thus, activities that are subject to the VAT tax include all activities, even single ones, that meet the criteria for being included in so-defined category of trade, that is organized sale of goods, preceded by their purchase made with the aim of re-sale, and whose characteristics indicate the intent of their continuation in this form. Nevertheless, the Court highlighted in

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<sup>5</sup> A commentary to Art. 15 of the Act of 11 March 2004 on value added tax (Journal of Laws No. 54 (2004), item 535), in: A. Bartosiewicz, R. Kubacki, VAT. Komentarz, Lex: 2007), second edition, *ibid.*

its decision that the condition for considering a person as a taxpayer is this person's constant involvement in the economic activity. Thus, it is reasonable to conclude that a natural person who is occasionally involved in a sale of goods must not be considered as a payer of the VAT tax. The Supreme Court of Administration also highlighted that, in accordance with Art. 4 passage 3 of the 6<sup>th</sup> Directive, Art. 12 passage 1 of the Directive 2006/112 (in force since 1 January 2007), and Art. 15 passage 2 of the Act of 11 May 2004 on the value added tax (Dz.U. [Journal of Laws] No. 54, item 535 with subsequent changes), henceforth called the VAT act, the occasional nature of an activity, or the single performance of an activity, leads to a person being considered as a taxpayer only in the case that such occasional or single activities are performed in relation to the activities of manufacturers, traders, or service providers, to include entities acquiring natural resources, and farmers, as well as to the activities of persons performing liberal professions. The aforementioned legal acts do not allow for taxation of activities, even if they can be defined as the sale of goods or provision of services in the understanding of Art. 7 and 8 of the VAT act, if they are not performed as a part of activities of manufacturers, traders, or service providers. On the other hand, a provincial court of administration concluded in its decision that not always a person's intent to perform an activity in a frequent manner will result in this person being considered as a VAT taxpayer. After all, the legislator had the intent to include only professional entities in the group of taxpayers of this tax<sup>6</sup>.

The opinions of tax authorities provide another important aspect. In its decision of 27 July 2007 (sign. 1438/VAT2/443–88/07/PG), the Warszawa – Ursynów branch of the tax authorities clearly indicated that the seller of six plots of land, separated from a farm that he had run for 25 years, will not be subject to the VAT tax because “the sale of the plots is taking place in circumstances indicating that this activity will not take the form of an organized activity and the plots had not been purchased with the aim of their re–sale.” What is immensely important in confirming the judicial decisions that have been made so far is the decision of the Warsaw court of administration<sup>7</sup> where the Court, deciding on a case concerning the taxation on a sale of a piece of real estate, concluded that the sale of plots of land by a person who is not conducting a registered economic company is not subject to the VAT tax. The Court stated that, according to Art. 15 of the VAT act, a given subject will be considered as a taxpayer, even when he performs the activity in an occasional fashion, as long as the activity will be related to the registered economic activity that he is conducting. In the justification, the Court pointed to the judicial decisions

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6 Decision of the provincial court of administration of 17 April 2007, sign. of the record I SA/Wr 123/07, “Rejent” 2007, No. 5, p. 182, see also the decision of the provincial court of administration of 26 January 2007, sign. of the record I SA/Wr 1688/06, “Przegląd orzecznictwa podatkowego” 2007, No. 2, item 34.

7 Sign. of the record III SA/Wa 1217/06, not published.

of the European Court of Justice, in particular to the decision of 26 September 1996 concerning the case no. C-230/94, where the ECJ stated that, in the understanding of the law on the value added tax, economic activity is defined as professional economic transactions. Consequently, professional transactions, from the point of view of the value added tax, are only those transactions that are performed by professional entities, i.e. entities that perform economic activity in the strict sense of this term. Such entrepreneurs are required to calculate the tax due and to pay it into the account of their branch of the tax authorities. Professional trade in property in Poland is subject to the basic rate of the VAT tax equal to 22%. The only exception is trade in buildings that belong to the category of housing buildings, which is defined as permanent dwellings classified in chapter 11 of the Polish Classification of Buildings. The construction and trade in such buildings is subject to a preferential rate of the VAT tax equal to 7%.

## Streszczenie

Zasadniczo, definitywnie, profesjonalny obrót majątkiem odnosi się do wykonywania działalności gospodarczej w celach zarobkowych, w sposób zorganizowany i ciągły. Jednak w regulacjach podatkowych nie zawsze pojęcie to odnosić się będzie do wykonywanej, rejestrowanej działalności. Konstrukcja systemu podatkowego dotyczącego opodatkowania czynności profesjonalnych wprowadza bowiem szczególne, różniące się od ogólnie przyjętej, definicje działalności gospodarczej dla własnych potrzeb podatkowych, przez co zdarzyć się może wykonywanie profesjonalnego obrotu majątkiem np. przez osobę fizyczną nieprowadzącą działalności gospodarczej w sposób zorganizowany i ciągły. Poniższy tekst ma przedstawić zasady opodatkowania profesjonalnego obrotu majątkiem w systemie polskiego prawa podatkowego z uwzględnieniem jego specyfiki na gruncie tych przepisów.