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Lax aspects in case of a property as a subject of taxation

S u m m a r y

A property tax is a levy on property that the owner is required to pay. The tax is levied by the governing authority of the jurisdiction in which the property is located; it may be paid to a national government, a federated state, a county or geographical region, or a municipality. Multiple jurisdictions may tax the same property. This is in contrast to a rent and mortgage tax, which is based on a percentage of the rent or mortgage value.

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The notion of property constitutes one of the most ambiguous categories, differently defined and interpreted depending on a given field of science. Analyzing legal provisions of the EU countries which regulate the issues of tax accounting and tax law, we may determine the general properties of elements of property. These are:

- Ability to generate future economic benefits;
- Reference to transactions or other events realized in the past;
- Remaining under control of the managing unit, which allows to enter them into the accounting system of a given entity.

Taking into account legal provisions of accounting, there are two categories of property (asset) elements: fixed assets and current assets.

The difference between current assets and fixed assets is important for the possible establishment of the tax collection point for the taxes whose taxation base is related to the subject resource. It seems that potential application of property-related tribute requires for the object of taxation to be easily identifiable, thus demonstrating certain regularity of its taxation. The review of the existing models of property tax shows that as far as tributes imposing burden on real estate are concerned, there is the primacy of building or land real estate over other types of property. It seems essential that the material property and intangible and legal values, as essential production factors of an enterprise, should constitute the main elements of the fixed assets structure.

To describe the real estate, the basic element of property, we should not only use the presentation of various ways of defining the notion of real estate by the lawmakers, but also take into account their features.

Analyzing legal aspects concerning real estate in the EU countries we may differentiate four elements which need to be taken into account when considering the forms and structures of property taxation. First of all, it is the immovability of real estate in time and space. The value of the real estate largely depends on the attractiveness of its location and the type of its use. Secondly, variety, manifested in the fact that there no two identical real estates. The factors that differentiate real estate are especially its area, shape, type of development, allocation in the spatial development plan, soil conditions, water conditions, utilities, neighborhood. That explains why there might be considerable differences between similar, but hardly comparable real estates. Thirdly – capital and time consumption with reference to industrial developed real estate. Limited financial resources allocated for purchasing the real estate depend on the investor's own resources and availability of external (foreign) finance. The indicated difficulties related to such investment are compensated by the long-term nature of the real estate enjoyed by the owner. A general rule states also that large capital consumption of the real estate usually results in its increasing value. Fourthly, the ability to satisfy particular needs,

which means that entrepreneurs are able to generate economic benefits. Each type of real estate has certain functions attached to it. In case of residential real estate – this may be economic, education, cultural, religious activity that can be run there. With reference to undeveloped real estate – conducting trading activities (the marketplace), services (parking lots), agricultural activity (arable land) and forest activity (forest land). Another consequence of possessing a real estate and the right to use it is the ability to generate measurable benefits. The type of benefit depends on the way of using the real estate.

The concept of property has never been defined in the Polish law system. In its wide sense, it is understood as total assets and liabilities belonging to a particular entity. Such definition of property is opposed to its narrow term denoting the estate which entails only assets. In the latter definition, debts do not belong to property, but lower its economic value. Also in economics the property is understood exclusively as a sum of assets – property resources controlled by an individual and possessing reliably defined value. These assets are divided into fixed assets, composed of elements that are permanently engaged in a given unit, and current assets, composed of elements which constantly traded. In this understanding of property, liabilities are treated as means of its origin, and when we juxtapose them with assets, we will obtain a balance sheet¹. In the legal sense, in the doctrine of civil law property has rather narrow meaning. This can be seen in the interpretation of the Civil Code provisions which use the concept of property – for example Article 863², 871³, 875 concerning joint property of partners. The provision of Article 863 is absolutely binding and regulates the legal and material effects of gathering property on the basis of articles of association of a partnership. The regulation determining the regime of joint property of partners is applicable when such property is collected.

The establishment of a partnership as an obligation relationship is self-contained and does not depend on whether the joint property of partners was generated. The collection of such property may, but does not have to, be the consequence of establishing a partnership. The joint property is a derivative of the relationship of partnership, though not all articles of association have to evoke such legal and material effects. We may assume the existence of a civil partnership within which

¹ L. Etel, G. Liszewski, *Podatki majątkowe w Polsce – wybrane problemy*, Kancelaria Sejmu, Biuro Studiów i Ekspertyz, Report No 202, Warszawa 2002, p. 5.

² Compare S. Grzybowski [in:] *System prawa cywilnego*, volume III, part 2, p. 812; K. Pietrzykowski [in:] K. Pietrzykowski, *Komentarz*, volume II, 2004, p. 561). Quoted after: Kidyba A. (ed.) Gawlik Z., Janiak A., Kopaczyńska-Pieczniak K., Kozieł G., Niezbecka, E., Sokołowski T., *Kodeks cywilny. Komentarz. Volume III. Zobowiązania – część szczegółowa*. Opublikowano LEX 2010, komentarz do art. 863 k.c.

³ Quoted after: Kidyba A. (ed.), Gawlik Z., Janiak A., Kopaczyńska-Pieczniak K., Kozieł G., Niezbecka E., Sokołowski T., *Kodeks cywilny. Komentarz. Tom III. Zobowiązania – część szczegółowa*. Opublikowano LEX 2010, komentarz do art. 871 k.c.

partners will oblige to act in a particular way, but none of them will be obliged to make any material contribution. Also the partnership activity will not generate any joint proprietary rights. Neither the establishment of the partnership nor its existence then is dependant, by the regulations, on the existence of joint property of partners. The provisions of Article 871 of the Civil Code determine the principles of settlement with a partner who leaves the partnership. They are applicable mostly when the partner leaves the partnership and withdraws their share observing the period of notice (Article 869 § 1 of the Civil Code) or not observing it (Article 869 § 2 of the Civil Code). Moreover, the principles of settlement provided in them are applicable in case of withdrawing one's share by a personal creditor of the partner on the basis of Article 870 of the Civil Code. It seems that unless the parties agree otherwise, also in case of articles of association of a partnership, on the basis of which a partner withdraws his share, the settlement with him should be conducted following the provisions of Article 871 of the Civil Code. In case of the partner's death, on the other hand, these provisions are used for settlement with their inheritors if they do not join the partnership in place of the late partner.

The provisions of the Civil Code do not regulate the principles of liquidating the partnership. However, activities undertaken after its dissolution, aimed at actually settling the partnership with its creditors and in relationship between partners, may, in some simplification, be treated as such. In commercial partnerships the appearance of the cause for liquidation in fact leads to opening the liquidation process, while the dissolution of a partnership becomes effective when the company is crossed out of the register following its liquidation. In case of civil partnerships, the order of events is different. The event that constitutes the cause for dissolving the partnership simultaneously causes its dissolution. On the other hand, the "liquidation" activities are conducted only after the termination (dissolution) of a partnership. The dissolution of a partnership is a legal event which needs to be analyzed in to major aspects. Most of all, the obligation relationship of a partnership expires. This means that all the rights and obligations of the partners as parties to the articles of association of this partnership also expire. Partners lose their status of partners as subjects of a legal relationship in the partnership. The second sphere in which partnership dissolution causes vital legal effects is the joint ownership referring to the joint property of partners. The joint ownership so far, at the moment of dissolving the partnership is by virtue of law transformed into ownership in parts. The provision of Article 875 § 1 of the Civil Code obliges us to apply to it the regulations concerning co-ownership in fractions, observing the provisions of Article 875 § 2 and 3 of the Civil Code. The dissolution of a partnership analyzed in these two aspects leads to a conclusion that the joint ownership in fractions, existing between former partners is self-contained. It exists in spite of the termination of a personal relationship (partnership relationship) between partners.

It is emphasized, though, that sometimes the lawmakers seem to be using the analyzed notion in its broad meaning – assuming that the inheritance is a kind of volume of estate, it should be admitted – following, for example, Article 922 of the Civil Code, that it consists of not only assets but also of many obligations the deceased person had (liabilities). Similarly, the wide understanding of “property” could also be seen in the interpretation of the provisions of Family and Guardianship Code concerning the management of a joint property of spouses. It is assumed though, that as a rule property is understood narrowly in Polish law.

The Civil Code regulates in Article 44 the term similar to “property”, that is “possessions”. The term is a collective name for all property rights (absolute and relative), both civil and other. The possessions thus are a subordinate (general) notion to particular property rights. Possessions cover only property rights (ownership and other property rights), that is the assets attributed to a particular entity. Therefore we should exclude from this term debts, that is liabilities which may only constitute a burden on possessions. The use of “ownership and other property rights” indicates the civil law rights. The ownership right is the broadest and the fullest civil right to things, other property rights are its derivatives. Thus the rights which are not of civil law nature, or the civil law rights of non-property nature, are located outside the scope of interest for Article 44 of the Civil Code, as they do not create possessions⁴.

Property should be differentiated from possessions, though there are numerous inconsistencies in using these terms in the Civil Code. There is a broader and a narrower understanding of the concept of property⁵. In its broader meaning, property denotes all property rights and obligations of a legal subject. In its narrow definition, property is associated only with assets, that is property rights possessed by the subject; such identification allows us to use the concepts of property and possessions interchangeably. Property are the elements of possessions which can be singled out as a collection of assets (or liabilities) being the object of trade, inheriting, security for liabilities, basis of responsibility for obligations, etc.

Property denotes property rights of a subject in a particular legal activity or another legal event. This can be a joint property (for example in case of spouses or civil partnership) and separate property (of spouses, in a commercial company and its partners), personal property (for example used to perform a job or personal belongings), property objects (for example in the property of spouses), property management (in co-ownership), responsibility for obligations related to

⁴ Kidyba A. (ed.), Gawlik Z., Janiak, A., Kopaczyńska-Pieczniak K., Kozieł G., Niezbecka E., Sokołowski T., *Kodeks cywilny. Komentarz. Volume III. Zobowiązania – część szczegółowa*. Opublikowano LEX 2010, komentarz do art. 44 k.c.

⁵ Pyziak-Szafnicka M. (ed.), Giesen B., Katner W.J., Księżak P., Lewaszkiwicz-Petrykowska B., Majda R., Michniewicz-Broda E., Pajor T., Promińska U., Robaczyński W., Serwach M., Świderski Z., Wojewoda M., *Kodeks cywilny. Część ogólna. Komentarz*. Opublikowano LEX 2009.

property, using the property (*inter vivos* and *mortis causa*). The elements of property are not objects whose rights they concern, but these rights due to the objects (for example real estate, moveable things). Similar can be said of the belongings.

Justifying property taxation we may refer to the principle of equivalence, the principle of payment capacity and principles and political and social rules of population income redistribution. The principle of equivalence is based on an assumption that there is a relationship between the amount of tax burden and the value of public goods and services provided for the taxpayer. Property tax is a good example of applying this principle. The state takes on the responsibility of protecting ownership rights, incurs expenses related to developing and maintaining economic infrastructure, tries to preserve social peace favoring full and free use of one's ownership. Local authorities take care of the roads, water and sewage systems, green areas, provide light in streets and keep the town tidy. Such activities not only allow to fully use the possessed property but also increase its market value. Due to the fact that most of the above-listed expenses are incurred by local authorities, property taxes mostly credit local budgets⁶.

On the other hand, the relationship between the amount of property taxes and payment capacity is mostly affected by the measures of wealth and related capacity to carry tax burden accepted by the society. Such a criterion can be the current income of a taxpayer, the level of their consumption expenses or gathered property, as thanks to the possessed property they may obtain higher current income. In contemporary tax structures it is usually income that is used as a measure of payment capacity. Both the structure and the amount of property tax rates depend on whether these taxes are treated as independent taxes, or as supplements to other taxes. Property taxes are usually treated as a supplement or correction of income tax in order to better reflect the taxpayer's payment capacity or to allow redistribution of incomes determined by social reasons. The economic effects of property taxation depend on the level of tax rates and on the object of taxation. Taxation of the property of individuals (for example cadastre tax, tax on estates and donations) performs mostly the redistribution function. Taxation of incomes from capital (dividends, interest on bonds, interest on bank deposits), apart from the redistributive function, also affects the willingness of capital owners to invest and save⁷.

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⁶ A. Krajewski, *Podatki. Unia Europejska, Polska, Kraje Nadbałtyckie*, PWE, Warszawa 2004, s. 112–113.

⁷ A. Krajewska, *Podatki ...*, op. cit., p. 114.

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