

Refund of gminas' revenues lost due to statutory reductions in local taxes and charges

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Summary: Currently, in Poland, there is a system of reimbursement of lost income, which is internally diversified. The legal institution of general subvention is used to some extent, as well as other ways of reimbursing lost income due to tax exemptions introduced by the legislator.

Keywords: tax relief, write-offs, the revenue of local government units.

Introduction

A characteristic feature of particular taxes and local fees is the existence of numerous legal titles justifying the application of reliefs and exemptions from taxation. They were introduced by the legislator exercising tax authority on behalf of the state. It follows from the provisions of Article 217 of the Constitution of the Republic of Poland [3] that the levying of taxes, other public levies, the determination of entities, subjects of taxation and tax rates, as well as the principles for granting reliefs and remissions and categories of entities exempt from taxes shall be based on law. The limits of the state's tax authority and the legal form of its exercise are jointly determined by Articles 217 and 84 of the Constitution of the Republic of Poland, indicating that the appropriate form in this respect is the law. The introduction of reliefs and exemptions, often for social and economic purposes, however, leads to a reduction in tax revenues and thus means a reduction of the capacity of local government units (LGU) to run

independent financial management. It also means that certain tasks of these units cannot be performed to the present extent while meeting local social needs is threatened.

The state's freedom in forming those structural elements of local taxes and charges, which result in lowering the level of own income of local government units, is limited. This is because guarantees have been introduced, primarily constitutional ones, which should constitute a safeguard for maintaining appropriate correlations between the scope of tasks imposed on the local government and the financial resources necessary for the proper performance of these tasks. In accordance with the provisions of Article 167 of the Constitution of the Republic of Poland, units of local government should be provided with adequate shares of public revenue to enable them to perform their tasks properly. Changes in the scope of tasks and competences of local government units may occur together with corresponding changes in the division of public revenues. It can be concluded that Article 167 of the Constitution of the Republic of Poland forms an integral whole. It provides local government units with a share in public revenue in accordance with their tasks. It indicates the types of income of local government units, including: own income, subsidies and purpose-specific subsidies from the state budget. It stipulates a statutory procedure for determining the sources of revenues, which constitutes an important guarantee of financial local government independence. Moreover, it stipulates that changes in the scope of tasks and competences of local government units shall be accompanied by corresponding changes in the distribution of public revenue [10, p. 37].

Specific guarantees concerning the basis for the financial management of the local government also stem from the provisions of ordinary laws. An example is the provisions of the Act of 6 May 2005 on the Joint Committee of Government and Local Government and on Representatives of the Republic of Poland in the Committee of the Regions of the European Union. The aforementioned Commission provides a forum for working out a common position of the government and the local government, as well as examines problems related to the functioning of the local government and the state policy towards the local government, as well as issues related to the local government that are within the scope of activities of the European Union and international organisations to which Poland belongs. The tasks of this Commission include reviews and evaluations of the legal and financial conditions for the functioning of local government, analysis of information on prepared drafts of legal acts, documents and government programmes concerning the issues of local government, in particular the expected financial effects, providing opinions on drafts of normative acts, programmes and other government documents concerning the issues of local government.

The Joint Committee shall deliver its opinion using a procedure to be agreed upon by

the two parties represented on the Committee, i.e., the government and the local government. The opinion may contain separate views on specific issues. If no agreement is reached, each party adopts its own position on the matter under discussion. Members of the Council of Ministers and other entities competent to prepare draft normative acts, programmes and other government documents concerning local government issues shall submit drafts of such documents, together with a forecast of their financial effects, to the Joint Committee for its opinion. The opinion of the Joint Committee on the drafts of these government documents shall be attached to them.

The introduction of new reliefs and exemptions from local taxes and charges may pose a particular problem for gminas in which the share of the revenue from these sources in own income is significant. The revenues from the property tax are of particular importance for the revenue potential of gminas. Due to the fact that the income potential of gminas is considerably diversified and the imperfect system of equalising the level of their income through the system of subventions and obligatory payments, the system of refunding lost revenues from tax sources will become more and more important. The fundamental difference between the system of equalisation of the revenue potential of gminas and the evolutionary system of refunding lost revenue is that under the equalisation system only partial coverage of the existing shortage of funds takes place, whereas under the refunding system it is complete coverage of the shortage caused by the application of certain reliefs and exemptions from taxation.

1. Reimbursement of lost revenue using the legal structure of subsidies

On 1 January 2004, a procedure was introduced to compensate gminas for the loss of revenue in connection with the application of statutory exemptions from real estate tax on land, structures and buildings, which are occupied for business activity within a special economic zone - on the basis of a permit, during its validity period [10, p. 52]. Such exemptions constitute regional public aid for supporting new investments. The amount of exemption is determined according to the state of the land, structures and buildings being the basis for the tax calculation for 2012 and according to the tax rates valid in 2012 in the given gmina. The gmina, which in a given tax year did not receive income as a result of such exemption, receives in the following year from the state budget a part compensating the general subvention for the loss of income resulting from the exemption - in the amount of this exemption. The amount allocated for the

compensation part of the subvention shall be determined for each budgetary year by the Budget Act, while the list of gminas entitled to the compensation part of the general subvention for the previous year and the method of determining and the procedure for transferring the amounts due shall be determined - by way of an ordinance - by the Minister competent for public finance in agreement with the Minister competent for the economy. The use of the legal institution of subsidies in this respect therefore means using mechanisms of vertical redistribution of public funds to balance the income potential of gminas [9, p. 98].

According to the provisions of this regulation, the amount of the compensation part of the subvention for gminas is established in the amount of the equivalent of the loss of income, resulting from the exemption from property tax of land, structures and buildings, occupied for conducting (within the special economic zone) economic activity by an entrepreneur on the basis of a permit. Gminas shall submit to the Minister responsible for public finance, by 10 May of the financial year, information on the expected amount of revenue loss in the financial year resulting from the exemption from property tax. The information should include:

- the basis for the real estate tax on land, buildings and structures occupied for the entrepreneur's business activity.
- property tax rates, according to the resolution of the gmina council, in force in 2012 the expected amount of loss of gmina revenue.

The loss of revenue is indicated in the gmina's application for the compensation part of the general subvention. The gmina is competent to determine the amount of revenue shortfall, but the verification of this determination is a task of the competent Regional Chamber of Auditors, to which the gmina submits the application by 25 August of the financial year - showing the annual effects of the property tax exemption as at 31 December of the year preceding the financial year. In the application the gmina shall indicate:

- the basis for the real estate tax, separately for land, buildings and structures, which in the year for which the application is prepared were occupied for business activity within a special economic zone, as of 30 November 2012,
- the property tax rates established by the gmina council, in force in 2012,
- the amount of the annual effects of the exemption from property tax determined as the sum of the amounts calculated separately for land, buildings and structures on the basis of the data referred to above.

The Regional Chamber of Auditors shall verify the correctness of the applications drawn up in terms of accounting and formal matters, and then forward them, by 10 September

of the financial year, to the Minister responsible for public finance, who shall, by 25 November of the financial year:

- informs the gminas of the amount of the compensation part of the subvention,
- shall transfer to the gmina budget account the amount of the subsidy compensation part determined on the basis of the application submitted on time.

The amounts of the compensation part are transferred to the gminas by 25 November of the year in which the gmina submits the application for the previous year. Thus, under the discussed procedure, the lost revenues from the real estate tax are fully refunded, and the source of financing of the revenues lost by the gmina is the state budget from which funds are transferred under the compensating part of the general subvention.

2. Reimbursement of lost revenue due to certain statutory exemptions from property tax

The Act of 12 January 1991 on local taxes and charges provides for a total of 23 titles of exemptions from property tax (16 exemptions of a subjective nature and 7 exemptions of a personal nature). All exemptions specified directly in the Act are applied by operation of law, i.e., without the need for a separate tax decision. However, the system of refund of income lost due to this reason was applied only to three statutory exemptions from property tax, i.e.:

- land located in areas under strict, active or landscape protection and buildings and structures permanently connected to the land and serving directly to achieve nature protection objectives in national parks and nature reserves,
- enterprises with the status of a research and development centre in respect of taxable objects occupied for the purposes of research and development work conducted,
- owned by the State Treasury: land covered by waters of lakes with continuous inflow and outflow of surface waters and/ or land occupied for artificial water reservoirs.

The first of the mentioned exemptions is a consequence of the amendment of the Tax Act by Article 134 of the Act of 16 April 2004 on Nature Conservation, in force since 1 January 2005. This exemption is conditional. First of all, it was allowed to apply it in relation to land in areas under strict protection, which means the complete and permanent abandonment of direct human interference in the condition of ecosystems, natural components and the course of

natural processes in areas under protection, and in the case of species - year-round protection of their individuals and stages of development. It is also necessary for such land to be located in national parks or nature reserves. With regard to buildings and structures permanently connected to the land, two conditions have also been formulated, the fulfilment of which together justifies exemption from taxation, i.e., they serve directly to achieve nature protection objectives and are located in national parks or nature reserves.

The latter exemption is also conditional as it covers taxable objects (land, buildings and structures) occupied for the purposes of research and development works conducted by entrepreneurs with the status of a research and development centre. The term "research" used above refers to several types of research, i.e., scientific, industrial and pre-competitive research. Within scientific research, a distinction is made between basic research (comprising research activities, experimental or theoretical - undertaken to acquire new knowledge of phenomena and facts, not directed towards direct application in practice) and applied research (comprising research activities undertaken to acquire new knowledge, capable of being applied in practice). Industrial research is planned research aimed at the acquisition of new knowledge which may be useful in developing new or substantially improving existing products, processes or services. The essence of pre-competitive research is to convert the results of industrial research into plans, assumptions or designs for new, modified or improved products, including the creation of a non-commercially usable prototype (this research does not include routine or periodic changes made to existing products, production lines, manufacturing processes, services and other operations, even if these changes represent improvements). Development work, on the other hand, is work that exploits existing knowledge in order to produce new or improve existing materials, products, devices, services, processes, systems or methods [5, p. 278].

An entrepreneur who is not a research and development unit may be granted the status of a research and development centre provided that:

- its net revenues from sales of goods, products and financial operations for the financial year preceding the year in which the application for such status is submitted amounted to at least the PLN equivalent of EUR 800 000,
- its net revenues from the sale of the results of the research or development generated by it constitute at least 50% of the abovementioned revenues,
- is not in arrears with payment of taxes, social security contributions and health insurance contributions.

The body authorised to grant the status of a research and development centre is the

Minister competent for the economy. The status is granted by an administrative decision.

Due to the aforementioned exemptions, the local government units are entitled to receive from the state budget the reimbursement of the lost income - according to the rules and procedures specified by the Minister of Finance by way of regulation [7]. This results from the need to secure gminas' budgets against the loss of revenue caused by the application of exemptions from the real estate tax. Pursuant to the Regulation of the Minister of Finance, the amount of lost revenue is indicated by the gmina in an application submitted to the competent voivode by 31 March of the year following the year in which the property tax exemption was granted. The application should indicate the actual annual effects of statutory exemptions (separately for land, buildings and structures), resulting from decisions and tax declarations, for the given tax year, as at 31 December of the year for which the application is prepared. In addition, the application must take into account the property tax rates set by the gmina council, in force in the year for which the application is prepared.

The gmina has the right to submit a correction of the application until 31 May of the year following the year in which the exemption occurred. The application or the correction of the application may also be submitted after the deadline, in connection with the correction of the tax return submitted by the taxpayer and in connection with the issuance of a new decision by the tax authority. An application or a correction of an application is subject to examination in the year following the year in which it was submitted. The competent voivode is responsible for verifying the correctness of the applications with regard to accounting and formal matters. By 31 August of the year following the year in which the exemption occurred, the competent voivode transfers to the gmina budget account funds equivalent to the amount of lost income due to the exemptions in question.

The Minister of Marine Economy and Inland Navigation, by way of a Regulation [8], has defined detailed rules and procedures for reimbursement to gminas of lost income in respect of exemption from property tax, owned by the State Treasury, of land covered by the waters of lakes with continuous inflow or outflow of surface waters and land occupied for artificial water reservoirs. Unlike the rules for reimbursement of the gmina's lost income from the two previously mentioned titles, in this case, the source from which the money for such purpose comes is different. The first of the discussed refunds takes place from the state budget resources, while the second one - from a special purpose fund, i.e., the provincial fund for environmental protection and water management. The lost income is reimbursed after the gmina submits an application - by 25 March of the year following the fiscal year - to the relevant Voivodeship Environmental Protection and Water Management Fund. The application

must show the actual annual loss of income resulting from the decision and the tax returns for the tax year in question as at 31 December of the tax year for which it is made.

The gmina may also submit a correction to the application by 15 May of the year following the fiscal year, which is subject to examination in the year following the year in which it is submitted. The disposer of the provincial fund shall check the application with regard to accounting and formalities by 15 April of the year following the fiscal year. If any defects or errors are found in the application, the gmina is requested to remove them within 7 days of the receipt of the request (if the defects or errors are not removed within this period, the application is left without consideration). The Fund shall transfer to the gmina budget account funds equivalent to the amount of lost income due to the discussed exemption, by 31 May of the year following the year in which the exemption occurred.

3. Refunding lost revenue due to certain statutory exemptions from agricultural and forestry tax

The Agricultural Tax Act (2019) sets out a total of 19 titles of tax exemptions (i.e., 12 subjective exemptions and 7 subjective exemptions). These exemptions may concern both the whole or only a part of an agricultural holding. However, only with respect to one exemption title, i.e., the one specified in Article 12(2), item 5a of the Tax Act. A mode of reimbursing gminas for lost income has been introduced. This refers to the exemption from agricultural tax of entrepreneurs with the status of a research and development centre with respect to taxable objects occupied for the purposes of research and development works carried out. This exemption has applied since 1 January 2006 and constitutes *de minimis* aid. Its introduction is one of a number of instruments that should encourage greater investment in research and development activities. One of the possibilities to support innovation is to increase the financial resources that can be used for this purpose in enterprises. In general, public authorities have two groups of instruments at their disposal in this respect:

- land (subsidies for innovation promotion),
- tax instruments.

It is worth noting that tax instruments allow enterprises themselves to assess which innovative activities give the best chance of economic success, while the system of grants focuses on priorities defined, often arbitrarily, by public authorities or even individual officials.

On account of the aforementioned exemption from agricultural tax, local government units are entitled to reimbursement of lost income from the state budget - in accordance with the rules and procedure laid down by the Minister of Finance, the amount of lost income is

specified in the application of the gmina, which is submitted to the competent voivode by 31 March of the year following the year in which the exemption from agricultural tax was set. The application must show the actual annual effects of the statutory exemptions resulting from decisions and tax declarations for the tax year in question, as at 31 December of the year for which the application is made. In the application, the gmina should indicate:

- the agricultural taxable amount for agricultural land which, as at 31 December of the year preceding the year in which the application is made, is exempt from that tax to the extent specified,
- the agricultural tax rates applicable in the year for which the application is being made,
- the amount of lost income established on the basis of the data listed.

The gmina may also submit a correction of the application until 31 May of the year following the year in which the exemption occurred. The application or the correction of the application may also be submitted by the gmina after the above-mentioned deadlines if it is connected to the correction of the tax return submitted by the taxpayer and to the issuance of a new decision by the tax authority. The application or a correction of the application are subject to consideration in the year following the year in which they were submitted. The competent voivode verifies the correctness of the applications in accounting and formal terms and, by 31 August of the year following the year in which the exemption occurred, transfers to the gmina budget account funds equivalent to the amount of lost revenue due to the exemption.

Analogous rules and the procedure for refunding revenue lost by gminas were applied with respect to forest tax exemptions under Article 7(2), item 6 of the Forest Tax Act - entrepreneurs with the status of a research and development centre, with respect to taxable objects occupied by them to conduct research and development work. This exemption from taxation constitutes *de minimis* aid. It is also the only case of reimbursement of gminas' lost revenue due to tax exemptions introduced by the legislator (apart from this exemption, the Forest Tax Act lists 5 other exemptions of a subjective nature and 3 exemptions of material nature).

Reimbursement of revenue lost by a gmina is made from state budget funds, according to the rules and procedure laid down by the Minister of Finance. The rules for the preparation of an application by a gmina, the deadlines for its submission to the relevant voivode and the transfer of funds to the gmina budget account by the voivode are identical to those for the refund of lost revenue due to the exemption of the same category of entities from agricultural taxation.

Conclusion

In each of the local taxes and each of the local fees (except for the administrative fee), the legislator introduces several to a dozen exemptions from the obligation to pay them by specific categories of entities. As a result of subsequent amendments to the acts regulating the legal construction of these public levies, the catalogue of exemptions is expanded. The economic effect of such exemptions is a reduction of revenues to gmina budgets from these sources. However, this problem cannot be analysed solely through the prism of the fiscal function of particular taxes and local fees. Many of the exemptions have been introduced in order to fulfil various social, economic and business functions. Their positive non-fiscal effects may become apparent only in the long term.

Only some of the tax exemptions have no negative financial impact on gmina budgets as a result of the applied system of reimbursement of gminas' lost revenues. The system of total refund of lost income has been adopted in this respect - however, it is limited only to some of the statutory exemptions. The basic source of financing of the refunding system are state budget resources and only in one case - resources coming from the provincial fund for environmental protection and water management. It is characteristic that the refund of the lost income occurs only after the end of the tax year in which the exemptions were applied.

Currently, the main burden of financing the system of refunding revenue lost by gminas lies with the state budget. However, this applies only to a few selected categories of exemptions in certain taxes (property, agricultural and forestry taxes). The solutions applied to date in this regard have little relevance to the overall financial management of gminas. The refund system does not cover all new, i.e. recently introduced, exemptions from taxation, e.g. those introduced on 1 January 2007 in inheritance and donation tax (it covers the acquisition of assets by a spouse, descendants, ascendants, stepchildren, stepfather and stepmother) or new personal exemptions from stamp duty for persons making notifications or submitting applications for official acts, or applications for certificates or permits (licenses, concessions), or submitting documents stating the granting of power of attorney or proxy, or their copies, extracts or copies, if they present a certificate on the use of social assistance benefits due to poverty: natural persons carrying out active species protection and natural persons whose agricultural, forestry or fishing farm is exposed to damage caused by protected animal species not covered by compensation from the State Treasury - only with respect to stamp duty items related to nature protection.

It may be expected that the system of reimbursement of gminas' lost revenues due to the application of statutory exemptions from local taxes and charges will cover further titles of exemptions. Gminas will certainly invoke the principle of the adequacy of financial resources and tasks resulting from the provisions of Article 167 of the Constitution of the Republic of Poland. This is because any depletion of gminas' financial resources from public sources should be associated with a corresponding reduction of the scope of tasks, the performance of which has so far been the gmina's obligation. If in such a situation, the scope of gmina's tasks is not reduced, the only appropriate solution will be the introduction, or actually the expansion, of a system of refunding lost gmina revenues.

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