

<https://doi.org/10.18778/1509-877X.2023.04.04>

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## EXIT TAXATION AND THE DTT BETWEEN POLAND AND BRAZIL

**Summary.** The article addresses the issue of double taxation elimination in cases involving the application of an exit tax under the DTT between Poland and Brazil, which was signed in 2022. The author explains the key characteristics of the Polish exit tax and then elaborates on an appropriate allocation rule in the context of exit taxation. The article also discusses Article 24 of the Polish-Brazil DTT, which deals with double taxation. Finally, the author presents the specific solutions adopted in other countries' double taxation treaties to eliminate double taxation in cases where an exit tax is imposed.

**Keywords:** exit tax, double taxation, emigration

### 1. INTRODUCTION

On 20<sup>th</sup> September, 2022, Poland and Brazil concluded the Agreement for the elimination of double taxation with respect to taxes on income and the prevention of tax evasion and avoidance (hereinafter referred to as

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“the Poland-Brazil DTT”). For the last decade in Poland, many provisions introducing tax institutions previously unfamiliar with Polish law have been implemented, especially in income taxation. As an example, in 2019, exit tax regulations entered into force. Since the Poland-Brazil DTT is one of the first treaties concluded after 2019, it is crucial to consider whether an issue of double taxation elimination after the imposition of exit tax was considered when establishing the wording of the analysed treaty. It must be pointed out that this problem concerns, in practice, taxpayers emigrating from Poland, as Brazil does not impose an exit tax.

## 2. POLISH EXIT TAX – KEY FEATURES

Capital and people mobility as well as the freedom of establishment encourage many taxpayers to change their residence or transfer their business assets abroad. This phenomenon impacts national budgets – some countries may lose their tax revenues. In addition, legislators face the dilemma of protecting tax claims against tax avoidance<sup>1</sup>. States can prevent this problem or ignore it. One of the methods of combating the effects of taxpayers’ emigration on the tax level is introducing a particular type of regulation, namely an exit tax. This tax is charged to taxpayers primarily when they leave the country of residence (i.e. in cases of emigration). It can be imposed on both natural and legal persons. In this case, the fiction is assumed that a taxpayer alienates their assets and is therefore obliged to pay tax on capital gains<sup>2</sup>.

Exit tax in Poland was introduced in 2019, in connection with the implementation of the Council Directive of 12<sup>th</sup> July, 2016, laying down rules against tax avoidance practices that directly affect the functioning of the internal market<sup>3</sup>. Generally, as stated under Art. 1 of the ATA Directive, this act applies only to taxpayers subject to corporate tax. However, along

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<sup>1</sup> L. de Broe, *Hard times for emigration taxes in the EC*, [in:] H.P.A.M. Arendonk, F.A. van Engelen, S.J.J.M. Jansen (eds.), *A tax globalist: the search for the borders of international taxation: essays in honour of Maarten J. Ellis*, Amsterdam 2005, p. 211; M. Nestmann, *op. cit.*, p. 551

<sup>2</sup> A. Nowak-Piechota, *Podatek od wyjścia – analiza i ocena regulacji*, “Przegląd Podatkowy” 2019, no. 1, p. 34.

<sup>3</sup> (EU) 2016/1164, Official Journal EU L 193 of 19.07.2016, pp. 1–14, hereinafter referred to as “ATA Directive”.

with the exit tax introduction to the Act on Corporate Income Tax<sup>4</sup>, the Polish legislator decided to establish similar provisions for natural persons<sup>5</sup>.

Taxpayers are subject to exit tax upon emigration or a transfer of certain assets abroad if Poland loses its right to tax capital gains on the alienation of their property and the transferred asset remains the ownership of the same taxpayer<sup>6</sup>. This tax is imposed on unrealised capital gains which are built-in business assets. Exceptionally, in the case of natural persons, private property [Pol. *majątek osobisty*], defined under the PIT Act, may be subject to exit tax (e.g. shares or interests in a partnership), provided that a person has been a Polish tax resident for a total of at least five years in ten years preceding the date of emigration<sup>7</sup>.

According to the Polish provisions, income is computed as a market value for the transferred assets at the time of exit, less their tax value at the time of departure<sup>8</sup>. This regulation ensures that the exit state (here – Poland) is entitled to tax the economic value of a capital gain created in its territory, although the gain was not realised before the transfer or emigration. In this case, an arm's length principle is applied when tax base is being established. The CIT and PIT exit tax rate equals, in principle, 19%<sup>9</sup>.

As a rule, taxpayers are obliged to pay the amount of exit tax assessed immediately. Exceptionally, the tax payment may be deferred by paying it in instalments over a maximum of five years (sometimes with interest and a guarantee). It concerns only transfers of assets or a change of residence within the European Union (and the EEA)<sup>10</sup>.

<sup>4</sup> Act of 15<sup>th</sup> February, 1992, on Corporate Income Tax (*Ustawa o podatku dochodowym od osób prawnych*), Journal of Laws PL 2022, heading 2587, amended, hereinafter referred to as: “the CIT Act”.

<sup>5</sup> Act of 23<sup>rd</sup> October, 2018, amending the Personal Income Tax Act, the Corporate Income Tax Act, the Tax Ordinance Act and certain other acts (Journal of Laws PL, heading 2193, amended).

<sup>6</sup> Art. 24f(2) of the CIT Act and Art. 30da(2) of Act of 26<sup>th</sup> July, 1991, on Personal Income Tax (*Ustawa o podatku dochodowym od osób fizycznych*), Journal of Laws PL 2022, heading 2647, amended, hereinafter referred to as: “the PIT Act”.

<sup>7</sup> Art. 30da(3) of the PIT Act.

<sup>8</sup> Art. 24f(5) of the CIT Act and Art. 30da(7) of the PIT Act.

<sup>9</sup> Art. 24f(1) of the CIT Act and Art. 30da(1)(1) of the PIT Act.

<sup>10</sup> Art. 24i of the CIT Act and Art. 30de of the PIT Act.

## 3. EXIT TAX AND ALLOCATION OF TAXING RIGHTS

Establishing an appropriate allocation rule under a particular double tax treaty for cases involving an exit tax is critical. From the perspective of both the emigration and the immigration state, two circumstances may give rise to a double taxation (or double non-taxation). The first country taxes an exit of unrealised gains, while the other taxes an actual sale and taxation of capital gains. In practice, the countries – parties to a particular treaty – may apply different provisions of that treaty that allocate taxing rights.

A distributive rule based on Art. 13 of the OECD Model Tax Convention on Income and on Capital (hereinafter referred to as: “the OECD Model”)<sup>11</sup> or the UN Model Double Taxation Convention between Developed and Developing Countries (hereinafter referred to as: “the UN Model”)<sup>12</sup> concerning capital gains is applied most in this case<sup>13</sup>. However, it must be noted that under this provision, the term “alienation” is used in all its paragraphs, whereas an exit tax is levied on deemed alienation of assets. The Convention does not define the term “alienation”. Thus, according to Art. 3(2) of the OECD Model, corresponding to Art. 3(2) of the UN Model, any term not defined in the Convention should have the meaning it has under the domestic law of the state applying a particular treaty. As a result, if the domestic tax law considers a deemed alienation as an alienation, Art. 13 of a treaty should be considered when an exit tax is imposed. Additionally, according to the OECD and the UN Commentary on Art. 13, the same rules should apply to capital appreciation of assets as in the case of the alienation of such assets<sup>14</sup>.

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<sup>11</sup> OECD (2017), *Model Tax Convention on Income and on Capital: Condensed Version 2017*, OECD Publishing, <https://www.oecd.org/ctp/treaties/model-tax-convention-on-income-and-on-capital-condensed-version-20745419.htm>

<sup>12</sup> UN (2021), *Model Double Taxation Convention between Developed and Developing Countries 2021*, United Nations, <https://financing.desa.un.org/document/un-model-double-taxation-convention-between-developed-and-developing-countries-2021>

<sup>13</sup> V. Chand, *Exit Charges for Migrating Individuals and Companies: Comparative and Tax Treaty Analysis*, “Bulletin for International Taxation” 2013, no. 4/5, [https://papers.ssrn.com/sol3/papers.cfm?abstract\\_id=2250769](https://papers.ssrn.com/sol3/papers.cfm?abstract_id=2250769) (access: 31.07.2023).

<sup>14</sup> Para. 9, first sentence: *Commentary on Article 13, Commentaries on the Article of the Model Tax Convention on Income and on Capital and Commentaries on the Articles of the United Nations Model Double Taxation Convention Between Developed and Developing Countries*.

Under the Poland-Brazil DTT, a distributive rule concerning capital gains is governed by Art. 14 of this treaty:

**ARTICLE 14**  
**Capital Gains**

1. Gains derived by a resident of a Contracting State from the alienation of immovable property referred to in Article 6 and situated in the other Contracting State may be taxed in that other State.

2. Gains from the alienation of movable property forming part of the business property of a permanent establishment which an enterprise of a Contracting State has in the other Contracting State or of movable property pertaining to a fixed base available to a resident of a Contracting State in the other Contracting State for the purpose of performing independent personal services, including such gains from the alienation of such a permanent establishment (alone or with the whole enterprise) or of such fixed base, may be taxed in that other State.

3. Gains that an enterprise of a Contracting State that operates ships or aircraft in international traffic derives from the alienation of such ships or aircraft, or of movable property pertaining to the operation of such ships or aircraft, shall be taxable only in that State.

4. Gains derived by a resident of a Contracting State from the alienation of shares or comparable interests, such as interests in a partnership or trust, as well as certificates or participating units of an investment fund, may be taxed in the other Contracting State if, at any time during the 365 days preceding the alienation, these shares or comparable interests derived more than 50 per cent of their value directly or indirectly from immovable property, as defined in paragraph 2 of Article 6, situated in that other State.

5. Gains from the alienation of any property other than that referred to in paragraphs 1, 2, 3 and 4 that arise in the other Contracting State may be taxed in that other State.

Considering the wording of Art. 14, it seems that Para. 5 may be a base to allocate taxing rights between the countries when exit tax is imposed (apart from the transfer of assets subject to an immovable property clause regulated under Art. 14(4) of the Poland-Brazil DTT). This approach may be confirmed in the Manual for the Negotiation of Bilateral Tax Treaties 2019 (hereinafter referred to as: “the Manual”)<sup>15</sup>. Paragraph 470 of the Manual concerning Art. 14(6) of the UN Model, which corresponds to Art. 14(5) of the Poland-Brazil DTT, states that some countries may use this provision to confirm their right to impose an exit tax provided under the domestic law on capital gains accrued

<sup>15</sup> <https://www.un.org/esa/ffd/publications/manual-bilateral-tax-treaties-update-2019.html>

before a change of residence. The Manual refers to the Commentary of the UN Model and Art. 1(3) of the UN Model Convention, according to which exit taxes are generally accepted in a tax treaty practice. However, a fundamental condition is that the tax liability in this case must arise before a transfer of residence. Additionally, this liability may not extend to income accruing after the change of residence.

As mentioned above, the analysed provision may be applied when the Polish exit tax is imposed on an emigrating taxpayer. Polish regulations in this regard meet the requirements stated in the Manual and the Commentary of the UN Model. According to Polish PIT and CIT provisions, the tax liability arises on the day preceding the day of the cessation of residence (or transfer of some assets abroad)<sup>16</sup>. Thus, a Polish taxpayer who emigrates to Brazil may seek the allocation of taxing rights based on Art. 14(5) of the Poland-Brazil DTT. It must be noted that, traditionally, Art. 13(5) of the OECD Model Convention (or Art. 13(8) of the UN Model), being an origin under both the OECD Model and UN Model to Art. 14(5) of the Poland-Brazil DTT, is governed by a residuary clause.

However, the Poland-Brazil DTT applied an alternative to the traditional wording of Art. 13(5) of the OECD Model Convention (or Art. 13(8) of the UN Model). According to Art. 14(5) of this treaty, either or both states may tax gains from the alienation of the property not mentioned in Art. 14 para. 1–4. Thus, the state of residence will eliminate double taxation under Art. 24 of the Poland-Brazil DTT.

It may seem that the implementation of an alternative distribution of taxing rights of a ‘sweep-up’ rule under Art. 14(5) of the Poland-Brazil Treaty may be preferable in the context of exit taxation. Additionally, it is the first Polish double tax treaty that modifies the traditional wording of the provision mentioned above based on the OECD or the UN Model. One may even conclude that this article was adopted in its current form to help emigrating taxpayers avoid double taxation resulting from the exit tax.

At first sight, the analysed construction of Art. 14(5) of the Polish-Brazil DTT allows for solving the double taxation problem under the treaty provisions. On the contrary, under the traditional wording of that provision, taxation rights are allocated exclusively to a residence state, which means that an emigrating taxpayer cannot apply the double taxation elimination method provided under the treaty.

<sup>16</sup> Art. 30da(6) and (7) of the PIT Act and Art. 24f(5) and (6) of the CIT Act.

For this reason, it is worth examining the possibility of applying Art. 24 of the Poland-Brazil DTT to the issues involving exit taxation.

#### 4. THE ELIMINATION OF DOUBLE TAXATION

Art. 24 governs the elimination of double taxation under the Poland-Brazil DTT.

##### ARTICLE 24

##### The elimination of Double Taxation

1. In Poland, double taxation shall be avoided as follows:

Where a resident of Poland derives income which may be taxed in Brazil in accordance with the provisions of this Agreement (except to the extent that these provisions allow taxation by Brazil solely because the income is also income derived by a resident of Brazil), Poland shall allow as a deduction from the tax on the income of that resident, an amount equal to the income tax paid in Brazil. Such deduction shall not, however, exceed that part of the income tax, as computed before the deduction is given, which is attributable to the income which may be taxed in Brazil.

2. In Brazil, double taxation shall be avoided as follows:

Where a resident of Brazil derives income which, in accordance with the provisions of this Agreement, may be taxed in Poland, Brazil shall allow, subject to the provisions of its law regarding the elimination of double taxation (which shall not affect the general principle hereof), as a deduction from the tax on the income of that resident, an amount equal to the income tax paid in Poland. Such deduction shall not, however, exceed that part of the income tax, as computed before the deduction is given, which is attributable to the income which may be taxed in Poland.

3. Where in accordance with any provision of the Agreement income derived by a resident of a Contracting State is exempt from tax in that State, such State may nevertheless, in calculating the amount of tax on the remaining income of such resident, take into account the exempted income.

Firstly, it must be remembered that an article of a treaty eliminating double taxation, based on the OECD Model or the UN Model (basically Art. 23A or Art. 23B), generally deals with double taxation caused by a conflict between residence rule in one country and source rule in another. Additionally, it may solve a concurrent conflict of residency rules that should be solved, in the first place, under Art. 4 of a relevant treaty<sup>17</sup>.

However, an imposition of exit taxes causes a *sui generis* non-concurrent conflict of residency rules. It stems from the fact that the tax liability under exit taxation arises when a taxpayer is a resident of an

<sup>17</sup> The OECD Commentary on Art. 23A and 23B, para. 4.

emigration country. In contrast, double taxation occurs when capital gains are realised in the new residence state. As Art. 24 of the analysed treaty does not address this type of conflict, it cannot be applied when an exit tax is imposed.

It can be argued that it is better to convert the unlimited tax liability that comes with an exit tax into a limited tax liability, as suggested by the OECD and UN Commentary on employment stock options. However, it is important to note that the provisions regarding employment income (Article 15 of the OECD and UN Model) and capital gains (Article 13 of the OECD and the UN Model) have different scopes. The first provision allocates taxing rights based on where the employment is exercised. This type of rule is not present in Art. 13 of the OECD and the UN Model, which means that this provision does not provide that the distribution of rights is dependable on the place of a taxpayer's residence when the gain occurred<sup>18</sup>.

Even though the proposed approach regarding the transformation of the tax liability may not be accepted, it does not provide an answer to a fundamental question: How should the source of capital gains be determined in this scenario? This issue is mentioned in the Manual. According to Para. 469 of this document, countries that adopt the alternative version of Art. 13(5) or (6) of a treaty should clarify during negotiations how the source of capital gain is to be determined. Otherwise, the emigrating taxpayer may face obstacles in receiving double tax relief in their country of residence.

An analysis of the Polish-Brazil DTT and official online documents, including the justification to draft legislation on ratification of the Poland-Brazil DTT<sup>19</sup>, indicates that this issue has not been addressed. Consequently, according to the Commentary on Art. 13 of the UN Model, Brazil's and Poland's domestic laws will determine the gain's source. However, as stated before, tax liabilities in emigration and immigration countries do not arise

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<sup>18</sup> V. Chand, *Exit Charges...*

<sup>19</sup> Draft Act of 26<sup>th</sup> January, 2023, on Ratification of the Agreement for the elimination of double taxation with respect to taxes on income and the prevention of tax evasion and avoidance, signed in New York on 20<sup>th</sup> September, 2022 (*Projekt ustawy o ratyfikacji Umowy między Rzeczpospolitą Polską a Federacyjną Republiką Brazylii w sprawie eliminowania podwójnego opodatkowania w zakresie podatków od dochodu oraz zapobiegania uchylaniu się i unikaniu opodatkowania oraz Protokołu do tej Umowy, podpisanych w Nowym Jorku dnia 20 września 2022 r.*), no. 2987.

concurrently. Thus, both Poland and Brazil may determine the source of the gain in a different way. This situation, again, may lead to double taxation.

It must be underlined that some countries with exit tax regimes implemented special modifications of Art. 13 in their tax treaties. These treaties grant an emigration state the right to levy an exit tax. In some treaties, there are directly adopted methods of eliminating double taxation for emigrating taxpayers. Most important is that these treaties stipulate that an emigration country may tax capital appreciation of shares and other interests for the residency period of a taxpayer in that country. Then, directly under the provision concerning capital gains taxation (mainly Art. 13), bilateral methods, eliminating double taxation, are implemented, i.e. exemption, step-up, or tax credit methods<sup>20</sup>.

Such a solution has been adopted in German tax treaty practice. As an example, Art. 13(6) of the German-Netherlands Income Tax Treaty that stipulates an exemption method, may be presented:

6. Where an individual was a resident of a Contracting State and has become a resident of the other Contracting State, the provisions of paragraph 5 shall not prevent the first-mentioned State from taxing under its domestic law the capital appreciation of shares, profit sharing certificates, call options and usufruct on shares and profit sharing certificates in and debt-claims on a company for the period of residency of that individual in the first-mentioned State. In such a case, the appreciation of capital taxed in the first-mentioned State shall not be included in the tax base when determining the subsequent appreciation of capital by the other State<sup>21</sup>.

On the other hand, the German-France Tax Treaty under Art. 7(6) regarding exit taxation contains a step-up clause:

6. Where an individual has been a resident of a Contracting State for a period of five years or more and has become a resident of the other Contracting State, paragraph 5 shall not prevent the first-mentioned State from taxing under its domestic laws any capital appreciation accrued, during the period of residence of that person in that State, in respect of shares in a company which is a resident of that State. If the first-mentioned Contracting State taxes an individual in respect of such capital appreciation, the other Contracting State shall, if it taxes the capital gains arising from a later alienation of the shares in accordance with paragraph 5, in determining the amount of the capital gains, use as the acquisition costs the value of the shares at

<sup>20</sup> A. Nowak-Piechota, *Podatek od wyjścia*, Łódź 2018, p. 180.

<sup>21</sup> Convention of 12<sup>th</sup> April, 2012, between the Federal Republic of Germany and the Kingdom of the Netherlands for the avoidance of double taxation and the prevention of fiscal evasion with respect to taxes on income, unofficial translation, IBFD Tax Research Platform (access: 30.07.2023).

the time of transfer of residence. If the sale price is less than the value of the shares at the time of transfer of residence, the sale price shall be taken into account in determining the capital gain by the first-mentioned State<sup>22</sup>.

The analysis of these exemplary provisions shows that implemented solutions primarily make it possible to determine a gain source. Accordingly, an unrealised gain arises in an emigration country and includes any capital appreciation during a taxpayer's residence period. In practice, such a solution is helpful in indicating the income that arises in the emigration country and, consequently, properly allocating the taxing rights.

## 5. CONCLUDING REMARKS

As stated in the Introduction, the Poland-Brazil DTT is one of the first treaties signed after the exit tax introduction in Poland. The Polish party had a chance to negotiate the treaty provisions allocating taxing rights due to the exit tax imposition on emigrating taxpayers.

This article's findings indicate that the implementation of the alternative version of Art. 13(5) based on the OECD Model (corresponding to Art. 13(8) of the UN Model) under the Poland-Brazil Treaty does not solve the problem of double taxation for cases involving exit taxation. However, it creates an opportunity to apply one of the double taxation elimination methods. Art. 24 of the analysed treaty does not resolve the non-concurrent residence-residence conflict. Consequently, a taxpayer emigrating from Poland may resolve double taxation issues only under mutual agreement, according to Art. 26 of the Poland-Brazil DTT.

In conclusion, in the author's opinion, Poland should have reconsidered a tax treaty policy to protect its emigrating taxpayers after introducing the exit tax<sup>23</sup>. Negotiating the treaty with Brazil was an excellent opportunity to achieve this objective, e.g. by inserting the step-up clause into an additional paragraph of Art. 14, following the tax treaty practice of the other countries. Unfortunately, this chance was wasted.

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<sup>22</sup> Convention of 21<sup>st</sup> July, 1959, between the Federal Republic of Germany and the French Republic for the avoidance of double taxation and the establishment of rules for reciprocal administrative and legal assistance with respect to taxes on income and on capital, business tax and land tax, unofficial translation, IBFD Tax Research Platform (access: 30.07.2023).

<sup>23</sup> A. Nowak-Piechota, *Podatek...*, pp. 185 et seq.

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PODATEK OD WYJŚCIA A POLSKO-BRAZYLIJSKA UMOWA O UNIKANIU  
PODWÓJNEGO OPODATKOWANIA

**Streszczenie.** Artykuł porusza problematykę eliminacji podwójnego opodatkowania w sprawach związanych ze stosowaniem podatku od wyjścia (*exit tax*) w ramach polsko-brazylijskiej umowy o unikaniu podwójnego opodatkowania podpisanej w 2022 r. Autorka przedstawia kluczowe cechy polskiego podatku od wyjścia, a następnie zastanawia się, jakie przepisy analizowanej umowy mogą mieć zastosowanie w przypadku obciążenia podatnika podatkiem od wyjścia. W artykule omówiono również art. 24 ww. umowy. Końcowo Autorka zaprezentowała specyficzne rozwiązania przyjęte w umowach o unikaniu podwójnego opodatkowania innych państw, pozwalające na eliminację podwójnego opodatkowania w razie nałożenia podatku od wyjścia.

**Słowa kluczowe:** podatek od wyjścia, podwójne opodatkowanie, emigracja