

2010 Brings Several Favorable Tax Changes

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COUNTRY DIGEST

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In 2009, Lithuania and other Baltic countries faced a difficult challenge combating financial instability. Lithuania increased most taxes to offset economic losses and bolster public finances in 2008-2009. However, 2010 has started with ease, as the tax burden has decreased. As a result, Lithuania remains attractive to foreign investors because of favorable tax planning opportunities.

Notably, the corporate income tax has dropped to 15 percent (from 20 percent). Moreover, small businesses that employ 10 or fewer employees and have annual income of LTL 500,000 or less are eligible for a special 5 percent corporate income tax rate (previously 13 percent).

Also, a new law prohibits the transfer of losses from 2009 and earlier between a Lithuanian resident parent company and its domestic subsidiaries.

Other 2010 tax developments are outlined below.

Complex Real Estate Agreements

Tax authorities, alerted to a series of complex financial transactions between related parties, have concluded that the transactions did not have a legitimate business purpose and were undertaken solely to decrease the main party's tax liability.

An individual acting on behalf of a Swiss company entered into a variety of agreements in which the same property was sold numerous times in order to artificially increase its value for tax purposes. The individual did not pay taxes on the sale or declare the income it received from a company in Lithuania.

The individual was assessed tax in the amount of LTL 1 million.

VAT

Starting this year, taxpayers may apply for a refund of VAT paid in other EU member states by filing an electronic form with local tax authorities in Lithuania.

The local tax authorities will forward the application to the tax administrator in the applicable EU member state.

Lithuania's VAT rate increased to 19 percent from 18 percent in January 2009 and to 21 percent from 19 percent on September 1, 2009.

During a transitional period that runs through December 2010, the 19 percent tax rate will apply for cigarettes and manufactured tobacco if the excise duty stickers for those products were ordered before September 1, 2009.

In July 2009 President Dalia Grybauskaitė signed a law introducing a reduced VAT rate of 9 percent for the heating of residential premises and water. The reduced rate will be in force through August 31, 2010.

Corporate Income Tax

In addition to the tax breaks for corporations and small businesses, the withholding tax on interest will be revoked if the interest is paid to legal entities registered or organized within the European Economic Area. The same rule applies for countries with which Lithuania has signed an income tax treaty.

As of 2010, a corporate tax exemption is available for budget-financed institutions; Lithuanian banks; state and municipal institutions, agencies, and organizations; state company deposit and investment insurance programs; and European Economic Interest Groupings.

Investment Projects

Until 2013, companies can take part in investment projects that offer attractive tax benefits. Companies can invest 50 percent of their profit into long-term assets used in the production of new products or services, to increase capacity, or to implement new processes and technologies, and the reinvested profit will not be included in the companies' taxable income. Investment in the replacement of production assets with similar new assets will not, however, be deemed a tax-beneficial investment project.

Personal Income Tax

The personal income tax rate in Lithuania remains at 15 percent. Dividends and other profit distributions also are taxed at a rate of 15 percent.

Amendments to the Law on Personal Income Tax came into force in August 2009. The law provides a complete list of benefits in kind and lists income that will not be classified as a benefit in kind for the tax period starting in 2010. The amendment to the Law on Personal Income Tax sets a new rule for the calculation of nontaxable income, a benefit that will no longer be available to members of non-limited liability companies.

Excise Duty

As of January 1, electricity is taxed by way of an excise duty. The amended Law on Excise Duty states that for one megawatt-hour of electricity, there will be two excise duties applicable: LTL 3.5 and LTL 1.8. A second excise duty of LTL 1.8 applies to electricity used for business purposes.

The excise duties on electricity apply to owners of excisable goods warehouses, registered and unregistered traders, and persons manufacturing or using excise-free energy products, alcohol, alcoholic drinks, or tobacco for purposes other than the established purpose. For imports, the excise duty is paid by the importer, provided that the imported goods are not brought to an excisable goods warehouse. The applicable tax base is the tax base of goods produced or imported in Lithuania.

Tax on Real Estate

Lithuanian tax authorities expect legal and natural persons to pay more than LTL 260 million on immovable property, which had to be declared by February 1, 2010.

According to the Law on Real Estate, if real estate is used by individuals for business or individual activities (with several exceptions) or is transferred to legal persons for longer than one month, it is subject to a 0.3 to 1 percent real estate tax calculated on the value

of the real estate. The council of the municipality or territory where the buildings and structures are located will determine the exact tax rate.

Lithuanian and foreign entities owning buildings and structures in Lithuania are required to pay real estate tax. The rate remains unchanged at 0.3 to 1 percent of the taxable value of buildings and structures.

The real estate tax return should be submitted to the state tax authorities within one month after the date of acquisition of the real estate. Legal entities (as opposed to individuals) should pay advance installments on a quarterly basis. Both individuals and legal entities should provide an annual real estate tax return to the state tax authorities by February 1 of the next year.

Tax Payments in Lithuania

Taxpayers are entitled to defer the payment of certain taxes for a period of one month to one year. Unpaid taxes are subject to a late payment fee. Late payment amounts no longer increase when the late payment is equal to the original debt amount.

The amount of tax penalties imposed depends on the type and period of noncompliance. Late filing of tax returns triggers penalties of no more than LTL 500 for the first violation. The second violation results in an increased penalty of up to LTL 1,000. In the event of tax evasion, the penalty is LTL 2,000 to LTL 4,000 if no criminal charges are filed.

A taxpayer is allowed to make voluntary corrections to a tax return for a five-year period after the payable term if an audit by the tax authorities has not commenced. This cancels any penalties pending for noncompliance. The taxpayer retains the right to apply for a voluntary correction to the tax return if an audit has commenced, but in that case, the tax authorities have the right to deny the application.

All decisions by the tax authorities may be appealed to the tax administrator, Tax Litigation Commission, and tax court. Decisions of the tax administrator may be appealed to the Tax Litigation Commission within 20 days of receipt of the tax administrator's decision. ♦

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