

Is Latvian personal tax due on dividends from Cyprus companies? (3/8/19)

On 4 January 2019, the Latvian State Revenue Service (SRS) issued a ruling on how the Personal Income Tax Act should be applied to dividends a Latvian tax resident individual receives from a company registered in Cyprus ("CyCo"). In the ruling, the SRS answers a question that remained unclear under the applicable law and the available legal interpretation.

Background

CyCo is wholly owned by the individual and distributes a profit arising after 2017 by paying him a dividend. Aware of recent substantial amendments to Latvian tax law, the individual asked the SRS to explain how certain provisions of the PIT Act should be applied.

Being tax resident in Cyprus, CyCo is subject to the general tax regime of Cyprus, under which a company's profits attract a 12.5% corporate income tax (CIT) in Cyprus. At the same time, CyCo may claim a statutory exemption under which its profit for 2018 attracts a 0% CIT. And the dividend paid to the non-Latvian resident individual is also exempt from PIT (or an equivalent tax) under the Cyprus tax regime.

Applying the PIT Act

Section 9(1)(2.1) of the PIT Act lays down two conditions that must be satisfied to exempt PIT on dividends (or equivalent types of income or deemed dividends):

1. Latvian CIT has been paid on them, or
2. foreign CIT (or an equivalent tax) has been paid or PIT (or an equivalent tax) has been withheld on them.

In applying this rule, it is assumed that either CIT or PIT has been paid if a dividend (or an equivalent type of income) is paid by a company that is registered in another EU/EEA country and operates under its domestic law.

Interpreting this rule grammatically leads to the conclusion that dividends an individual receives from a company registered in an EU/EEA country qualify for an exemption whether or not tax has actually been paid in that country, i.e. based solely on where the company is incorporated and carries on business.

The SRS's interpretation

Under section 9(3.6) of the PIT Act, the SRS finds that Latvian PIT is no longer due on dividends an individual receives from a Cyprus-registered company organised and existing under Cyprus law out of profits arising after 2017 because it is assumed that CIT or PIT has been paid. In the case of dividends paid by EU/EEA companies, the question of whether either tax has actually been paid is ignored.

This implies that the situation in which neither CIT nor PIT has actually been paid by the EU/EEA company on dividends it pays to the individual is not an exception to the general rule that exempts both CIT (by means of reducing the amount of dividends included in the taxable base for the tax year) and Latvian PIT

on dividends received from foreign companies.

Key takeaways for taxpayers

Under administrative procedure rules, a ruling is issued to a particular person of private law. Another taxpayer seeking to verify the application of a particular provision of law in his actual circumstances should write a letter to the SRS, asking his own question and setting out his facts. Having assessed those details, the SRS will issue a new ruling addressed to that person.

This exemption will not apply if the SRS finds that the parties to the transaction have created an artificial arrangement under the Latvian Cabinet of Ministers' Regulation No. 677, *Application of provisions of the Corporate Income Tax Act*, paragraph 55 and Appendix 5(2).

¹ SRS ruling No. 31.1-8.5/2751 of 4 January 2019