Brexit: corporate tax implications (2/11/19)

There are about ten days left until the UK presumably leaves the EU. An event of such a magnitude is bound to have tax implications. Clearly, VAT and customs are the most affected taxes, yet the corporate income tax (CIT) treatment will also change. This article explores how Brexit will affect a few situations we have picked for review.

A 3% CIT to be withheld on the sale of real estate (RE)

If a foreign company sells either RE in Latvia or shares in a company with Latvian RE making up more than 50% of its asset profile, then a 3% CIT should be withheld on the proceeds. This rule does not apply to income arising on the sale of EU publicly traded securities.

For example, if a UK holding company sells shares in a Polish company whose subsidiary owns RE in Latvia, which are listed on the London Stock Exchange, the UK holding company will have to suffer a 3% CIT on the selling price paid indirectly for the shares in the Latvian company. Any UK listed securities will no longer be treated as EU publicly traded securities after Brexit.

Since Brexit has no effect on double tax treaties (DTT), UK companies can still file a statement of tax calculation with documentary evidence of their expenses associated with their RE revenues, and elect to charge a 20% CIT on their profits.

Loss of income from assigned receivables

Any loss a taxpayer suffers under a debt assignment contract is part of their non-business expenses. An exception to this rule applies to member states and countries that have an effective DTT with Latvia.

For example, a Latvian company sells a portfolio of receivables carried at €500,000 to a UK company for €380,000. The debt assignment rules under the CIT Act will still apply to UK companies after Brexit, so the Latvian company's loss of €120,000 can be excluded from its CIT base.

Doubtful debts

If a provision for a bad debt (after expiry of a 36-month period) or an expensed receivable is to be excluded from the CIT base, the debtor must be a company established in a member state or in a DTT country.

A provision the Latvian company made for a UK receivable in December 2018 can be excluded from its CIT base in December 2021 if all recovery procedures have been completed in the meantime and another one of the conditions laid down by section 9(3) of the CIT Act is met.

Thin capitalisation rules

If a Latvian taxpayer's average interest charges on borrowings from a UK financial institution exceed four times the shareholders' equity appearing on the annual report at the beginning of the financial year but does not reach €3 million, those interest charges can be excluded from the CIT base because the UK finance provider is still a taxpayer established in a DTT country.

However, if bonds issued by a Latvian company are listed on the London Stock Exchange, then any interest charges exceeding four times the shareholders' equity or €3 million will have to be included in the thin capitalisation assessment and also in the CIT base. Those bonds will no longer be treated as EU/EEA public securities.

Donations

Brexit will also affect donations the Latvian company intends to make to a UK non-governmental organisation. A taxpayer may donate to a foreign non-governmental organisation registered in another EU/EEA country that has an effective DTT with Latvia.

This is an overview of just a few situations to be affected by Brexit. We will soon be writing about its effect on arrangements involving UK companies or partnerships.