

Dividend payment: Is PIT relief available to individual if company has claimed CIT relief?

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Senior Consultant, Tax, PwC Latvia
Madara Hmelevska



Director, Tax, and Head of Pan-Baltic
People and Organisation Practice, PwC
Latvia
Irena Arbidane

To pick up where we left off in our earlier article [Ways of reducing tax on profit distribution](#), which discusses how to minimise your corporate income tax (“CIT”) liability when distributing “new” profits, this article explores some personal income tax (“PIT”) relief an individual can take even if the company has already claimed one of the available CIT reliefs according to the current practice.

The legal framework

[Section 9\(1\)\(2.1\) of the PIT Act](#) provides that dividends, dividend equivalents and deemed dividends are excluded from an individual’s taxable income for the year and exempt from PIT if one of the conditions below is met at company level on the portion of profit out of which the dividend is paid:

1. Latvian CIT has been paid under [the CIT Act](#).
2. Foreign CIT or PIT (or an equivalent tax) has been paid, or the company is registered in an EU or EEA country. This provision does not apply if the payer of income is based, established or incorporated in a blacklisted tax haven.

[Section 9\(3.8\)\(1–2\) of the PIT Act](#) specifies two cases where PIT relief is not available:

1. Dividends are paid to avoid or reduce PIT payments through an arrangement which, after considering all the facts and circumstances (the economic content and substance of the taxpayer’s transactions as well as their legal form being considered for tax purposes), is found to have been artificially created.
2. If the dividend were paid to the taxpayer directly from its source it would attract a higher rate of PIT than if it is paid through an arrangement or a series of arrangements.

So despite the CIT exemptions at company level mentioned in our [earlier article](#), the shareholders – individuals – are not subject to PIT if dividends are paid out of the Latvian company’s profits for 2018 or later years and the company has not used tax planning to achieve full or partial evasion from PIT. This is confirmed by [paragraph 35.1 of the Cabinet of Ministers’ Rule No. 899](#), which states that a PIT exemption is available if the CIT payer who is paying dividends has been permitted to deduct those dividends from ones included in the CIT base as required by the CIT Act.

[Paragraph 35.3 of Rule No. 899](#) provides, however, that a PIT exemption is not available if the CIT base has been reduced according to the conditions for excluding income on share disposal from the tax base under

section 13 of the CIT Act. So the company can reduce the dividends included in the tax base for the tax period to the extent it has gained income in the tax period from the disposal of direct participation shares held for at least 36 months at the time of disposal. The CIT base cannot be reduced if –

1. the company whose shares are disposed of is based, established or incorporated in a tax haven;
2. the disposal involves shares (other than publicly traded stock) where real estate in Latvia represents more than 50% of the company's asset value in the year of disposal or in the previous financial year, and no part of the income attracts PIT;
3. the disposal involves shares in investment funds and alternative investment funds;
4. the company whose shares are disposed of has been created or exists, or the transaction is made, for the main purpose of claiming a tax exemption.

Summary

| Criteria | Conditions | PIT treatment of dividends | CIT relief |
|---|--|----------------------------|--|
| Latvian CIT has been paid under the CIT Act. | Dividends are paid out of profits for 2018 or later years and the company has not used tax planning to achieve full or partial evasion from PIT. | No | See the list of reliefs in Available relief (Ways of reducing tax on profit distribution) |
| | | Yes | Section 13 of the CIT Act: income arising on the disposal of shares is excluded from the CIT base if they were held for 36 months. |
| CIT or PIT (or an equivalent tax) has been paid in a foreign country other than a tax haven, or the company is registered in an EU/EEA country. | | No | N/A, according to foreign law |

A practical example

The table below compares the tax treatment in two cases where a company has decided to pay a dividend of EUR 300,000 and has taken one CIT relief:

1. EUR 15,000 was donated to a public benefit organisation in 2020;
2. There was a disposal of shares the company had held for 40 months. Proceeds from disposal EUR 100,000, share acquisition cost EUR 40,000, profit EUR 60,000.

| | 1. The CIT base is reduced by 85% of the donation but not to exceed 30% of the CIT charge on dividends | 2. The CIT base is reduced according to the conditions for excluding share disposal income from the tax base |
|---|--|--|
| Profit (entire 2020 profit is distributed in dividends) | 300,000 | |
| CIT charge without relief | $(300,000 / 0.8) \times 20\% = 75,000$ | |
| Donation in 2020 | 15,000 | - |
| CIT on donation | $15,000 / 0.8 \times 20\% = 3,750$ | - |

| | | |
|--|---|---|
| Profit on share disposal (held >36 months at disposal) | - | 100,000 - 40,000 (acquisition cost) = 60,000 |
| CIT relief calculation | 15,000 x 85% = 12,750 (below 30% of 75,000, i.e. 22,500) | (60,000 / 0.8) x 20% = 15,000 |
| CIT due after taking relief | 75,000 + 3,750 - 12,750 = 66,000 | 75,000 - 15,000 = 60,000 |
| Individual chargeable to PIT | No | Yes 60,000 x 20% = 12,000 PIT is only due on the portion of profit that has not been charged to CIT. |
| Overall tax burden | 66,000 | 72,000 |

So given the cap on PIT relief where the CIT relief for share disposal has been taken, the reduction in the overall tax burden will be quite small (EUR 75,000 versus 72,000). The CIT relief on donations offers a greater reduction in the overall tax burden.