

Management and consulting services (3/29/21)

We have written earlier about the corporate income tax (“CIT”) treatment of payments made to a non-resident company on which tax must be withheld under section 5 of the CIT Act. This article explores the legal framework, examples and supporting documents for the most common type of payment: management and consulting fees.

The legal framework

Section 5(5) of the CIT Act defines the term “management and consulting services” as a set of activities the non-resident company performs either directly or through contractors to carry out the running of a Latvian-resident company or of another non-resident company’s permanent establishment in Latvia, or to provide them with any advice they need.

Since consulting services include a variety of activities, paragraph 30 of the Cabinet of Ministers’ Rule No. 677 of 14 November 2017 explains that services are treated as consulting services on the basis of their economic content and substance, not only their legal form, including preparation of various types of documents (calculations, projects, and business plans), supply of information on changes in accounting software, market research and advertising, in production equipment and technology markets, and on other matters related to the trader’s strategic development, production and sales, or research into the trader’s economic activities.

So, in each particular case you need to assess whether the non-resident company’s services (activities) can, according to their economic substance, be treated as consulting services within the meaning of CIT rules based on the principle of substance over form. If there is any doubt as to whether the non-resident company’s services qualify as consulting services for CIT purposes, we recommend seeking a tax ruling from the State Revenue Service to avoid any tax risk.

Examples

Since the term covers a variety of services, we have put together several types that are and that are not treated as management and consulting services within the meaning of the CIT Act:

YES

Management services
Consulting services
Legal advice
Preparing various types of documents (calculations, projects, and business plans)
Services involving supply of information on changes in accounting software, market research and advertising, and in production equipment and technology markets
Advice on marketing strategy and ways of placing advertisements
Services on various matters related to the trader’s strategic development, production and sales, or research into its economic activities

NO

Testing and certifying sample goods (such as analysing a sample, examining its chemical composition, performing technical checks, issuing a certificate etc)
Legal services limited to performance of legal activities, such as registration, drafting contracts, taking part in litigation, protecting legitimate interests, settling disputes out of court, and preparing legal documents for the courts
Upskilling courses
Advertising services
Technical engineering services
Brokerage services in finding a buyer

Supporting documents

Every company must have supporting documents in place that not only explain the economic substance of services it acquires but give a true and fair view of whether the services can, according to their economic substance, be treated as management and consulting services within the meaning of CIT rules, and those services must be related to the company's business.

For example, if the non-resident company's invoice refers to "management services" or "consulting services" and there are no other supporting documents available, this poses a tax risk. You need clarity as to what services have been rendered, for how many hours, and at what hourly rate - these details can be included in a contract, invoice or other mutually accepted document because only this can provide an understanding of the economic substance of the transaction. If the non-resident company has rendered various types of services, including consulting, then to avoid the risk of having to withhold tax on the whole invoice, the total fee should be split according to the particular types of services and the invoice should describe those services and break the fee down into relevant amounts.

You also have to comply with CIT rules relating to the taxation of payments made to non-residents and any available relief.