

Do payments between persons living together attract income tax? 3/50/21



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On 8 November 2021 Liepaja District Administrative Court heard a petition (case A42-02059-21) to overturn a State Revenue Service (SRS) decision assessing X (the petitioner) to extra personal income tax (PIT), a late fee and a penalty for undeclared income from person Y, who actually lives with X as they take care of each other and their child without entering into a marriage.

Background

In 2018 X received remittances from Y totalling EUR 8,855 with or without comments on the purpose of payment. The persons are not related by blood or marriage, nor do they share a declared address. Y periodically stayed and worked abroad. An examination of X's bank account movements did not suggest the money had been spent solely to maintain their child or household, as X had made payments at various retail outlets and deposited money into a savings account. No utility payments were made to maintain their shared household during that period.

The SRS's view and the relevant law

Section 9(1)(35) of the PIT Act exempts gifts up to EUR 1,425 a year from individuals to whom the taxpayer is not related by marriage or by blood up to the third degree defined by the Civil Code.

Accordingly, if persons living in an unregistered union make regular payments to each other and the total for the year exceeds EUR 1,425, the excess attracts PIT.

This rule applies not only to unregistered unions but also to other gifts made to non-relatives (e.g. assistance to foster parents). So those persons, too, have to declare gifts up to EUR 1,425 a year as exempt and any excess as taxable, requiring payment of PIT.

The court ruling

The District Administrative Court decided to grant the taxpayer's petition and overturned the SRS's decision assessing the extra PIT, late fee and penalty. The ruling stated that the SRS should have found no grounds for discriminating between a family of two married persons with a child and two persons actually living together and taking care of each other and their child.

The court found it important that X sees this union with Y as a family with a joint budget. The court observed that Y had stated X's declared address as his residence address when receiving banking services and claiming unemployed status, which may imply that they share a household. Y had also entered this address on documents filed with a foreign tax board. So the court had no doubt that Y stated this address as his residence.

The court finds that the provisions of the PIT Act have been applied narrowly, without looking into the circumstances of the case, so the SRS's decision charging the tax, late fee and penalty must be overturned.

The ruling suggests that the court broadens the scope of the PIT Act. Unless the ruling is appealed, we believe the Ministry of Finance should consider amending the PIT Act to broaden its treatment of gifts within a household and ensure they do not create taxable income.