# Corporate tax treatment of non-resident investment fund selling shares in Latvian “real estate company” 1/37/22

Investment funds have recently become more active in Latvia. Foreign non-resident investment funds often invest in the share capital of Latvian companies. The Corporate Income Tax (CIT) Act is silent on the CIT or personal income tax treatment of a non-resident investment fund paying income to its non-resident members from the sale of shares in a Latvian-registered company. Following the “Advise First!” principle of the State Revenue Service (SRS), PwC has prepared an application on behalf of a client seeking an advance tax ruling on how to proceed in this case.

## Background

The applicant is an investment fund resident in a country that has an effective double tax treaty with Latvia. The investment fund does not have legal entity status under the law of its residence country.

The investment fund is represented by its management company. The rights, liabilities and assets of the fund are separated from those of the management company. The income of the fund members is taxed when it distributes profits to, or buys back its shares from, its members.

The applicant is planning financial investment in Latvia by investing cash in the share capital of X SIA, a newly formed private limited company. The applicant will be the sole shareholder in the company, with real estate in Latvia representing more than 50% of its total balance sheet assets.

Contemplating a subsequent sale of shares in X SIA, the applicant wants to know who will have an administrative obligation to withhold and pay CIT on a future share disposal.

## The applicable tax rate

Section 5 of the CIT Act determines a non-resident entity’s taxable items, the tax rate, and the proper tax withholding procedure.

Section 5(1)(2) of the CIT Act states that any revenue a non-resident gains from real estate in Latvia, including revenue from selling shares or other type of participation specified by section 5(2), represents taxable income for the non-resident, and the payer of income must withhold a 3% CIT on the price paid.

A taxpayer resident in an EU member state, or in a country that has an effective double tax treaty with Latvia, who gains the revenue specified by section 5(1)(2) of the CIT Act has an option to file with the SRS a statement of CIT calculation, considering the expenses associated with that revenue, and charge a 20% CIT on taxable income.

## The withholding obligation

Under section 5(7.1) of the CIT Act, if an investment fund or an alternative investment fund is a Latvian tax resident then the asset management company or the alternative investment fund manager that settles with the non-resident member of the fund is responsible for withholding and paying tax on the disposal of the real estate company.

The CIT Act is silent about an (alternative) investment fund being a non-Latvian resident. So we asked the SRS whether section 5(7.1) of the CIT Act applies in this particular legal situation.

The advance tax ruling states that although in this case the alternative investment fund manager is non-resident, the asset manager is responsible for withholding and paying tax on payments specified by section 5(1)(2) of the CIT Act which the non-resident receives as a member of the alternative investment fund.

So the fund member is the payer of tax, but the fund manager is responsible for withholding and administering tax on behalf of the fund.

## Remember!

An advance tax ruling only serves as a source of information in interpreting provisions of law for other taxpayers. The SRS is bound by the ruling only against its addressee, so we recommend assessing each potential transaction separately on its merits and asking the SRS to issue a separate ruling.