

Payments to non-residents (3/34/20)

The **Corporate Income Tax ("CIT") Act** requires Latvian residents (other than individuals) and permanent establishments to withhold tax on certain payments made to non-residents. This article explores key aspects of the withholding tax treatment.

Taxable items and rates

CIT must be withheld on payments that residents and permanent establishments make to non-residents unless personal income tax has been withheld on them. **Section 5 of the CIT Act** lists a non-resident's taxable items and tax rates:

Taxable item	Rate
Management and consulting fees	20%
Consideration for selling real estate in Latvia	3%
Consideration for leasing real estate in Latvia	5%
Payments to persons that are based, formed or established in tax havens	20%

Although Latvia's double tax treaties provide for withholding Latvian tax also on other payments to non-residents (such as interest and royalties), Latvia offers a more generous treatment and tax must be withheld only on payments listed by the CIT Act.

In practice, it is important to remember that management and consulting services are a set of activities that a non-resident carries out, whether directly or through contractors, to ensure a taxpayer's management or to provide them with any advice they need. A service is classified as a consulting service according to its economic content and substance, not only its legal form, including the preparation of various deliverables and materials (calculations, projects, business plans), providing information on changes to accounting software, market research and advertising, equipment and manufacturing technology markets, and other matters related to the taxpayer's strategic development, manufacturing and sales, and research into the taxpayer's business activities.

Consideration for selling real estate in Latvia includes income from selling shares or any other interest in a Latvian- or foreign-registered company or another entity if real estate in Latvia represents or represented more than 50% of the company's asset value, whether directly or indirectly (through participation in one or more other Latvian- or foreign-registered companies) in the financial year of sale (with the exception of shares being sold in the course of a reorganisation specified by **section 18** of the CIT Act) or in the previous financial year.

Exemptions

If Latvia has an effective double tax treaty with a particular country, residents may be released from the obligation to withhold tax on management and consulting services by obtaining a residence certificate as prescribed by **the Cabinet of Ministers' Rule No. 178 of 30 April 2001**. An exemption can be claimed if a residence certificate is received before the tax return for the last month of the financial year is filed. We suggest finding out more about **proposals for amending Rule No. 178**.

Where tax must be withheld, the liability may be reduced by a taxpayer resident in an EU member state or in a country that has an effective double tax treaty with Latvia. A qualifying taxpayer may file with the State Revenue Service ("SRS") a statement and documentary evidence proving the amount of expense related to the revenue, and charge a 20% tax on the taxable income. A reduction in the tax charge arises because the payer is initially required to withhold tax on the amount of payment, but the legislation allows the payee to utilise the related expenses and pay tax only on the Latvian-source profit.

Paying tax and notifying the SRS

Tax must be paid either at the time of payment or, if tax was not withheld and there are no grounds for an exemption, tax must be paid when filing the CIT return for the last month of the financial year. Where tax should have been withheld and paid to the government but this was not done, the taxpayer must increase the CIT liability by the tax due on the non-resident's income after dividing it by a coefficient of 0.8 and multiplying by the appropriate rate.

A payment must be reported on or before the 20th day of the following month if CIT must be withheld on the payment at source. Any other payments to non-residents (even if the payer was eligible for an exemption under a double tax treaty) must be reported to the SRS at the time of filing the CIT return for the last month of the financial year. The SRS must be notified if a non-resident's relevant payments total more than EUR 5,000 for the year.