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Baltic dividend taxation differs for individuals residing in country with traditional system 1/21/21


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Effective from 1 January 2018 the Latvian tax system has undergone important changes affecting the taxation of personal income, including dividends. This article examines some of the changes in the tax treatment of dividends from Latvian sources and their impact on Latvian, Estonian and Lithuanian taxpayers.

Treatment before 2018

Latvian-source dividends were taxed at two levels. First a 15% corporate income tax ("CIT") was levied on the Latvian company's profit for the tax year, and a 10% personal income tax ("PIT") was then withheld from the payment to a Latvian or non-Latvian tax-resident individual. For example, a profit of EUR 100 for the year had a CIT charge of EUR 15 deducted from it, leaving only EUR 85 to be distributed by board resolution. A Latvian, Estonian or Lithuanian resident ended up with EUR 76.5 (85 less 10%) meaning the Latvian company's profit available for distribution was taxed at an effective rate of 23.5%.

Treatment after 2017

CIT and PIT are bundled into a single new CIT charge on dividends paid out of profits arising after 2017. Charged at 20% on a dividend declared by the board of directors, the liability is then divided by 0.8 so the effective rate on the distributed dividend is 25% (an increase of 1.5 percentage points).

Under the Latvian PIT Act, dividends are taxed at a rate of 10%, 20% or 0% subject to three conditions:

	Condition 1: the year profits are generated	Condition 2: chargeable to PIT or CIT in Latvia or elsewhere	Condition 3: set up for tax evasion
0%	Profits earned after 2017 (qualifying distributions) may be zero-rated for Latvian PIT unless other conditions apply. Profits generated by a microbusiness taxpayer after 2020	PIT or CIT has been paid on qualifying distributions from a Latvian or EU/EEA company. If the paying agent is located elsewhere a zero-rating depends on documentary evidence showing that PIT or CIT has been deducted at source. Exception: tax-haven companies	No
10%	Dividends paid in 2018 or 2019 out of a Latvian or foreign company's profits generated before 2018 will attract a 10% PIT.		

20%	Profits earned before 2018 will attract a 20% PIT if paid out either after 2019, or by a microbusiness taxpayer before 2021.	No PIT or CIT has been charged, or the profit is distributed by a tax-haven company.	If tax authorities consider so, a 20% PIT will apply regardless of other conditions.

Non-Latvian tax residents

The Latvian company paying a dividend will effectively pay a 25% CIT (no PIT) so a non-Latvian resident will receive the gross dividend. The tax payment methodology is the same for Latvian and non-Latvian tax residents.

For example, a Latvian company's board declares a dividend of EUR 10,000. The company will pay a CIT charge of EUR 2,500 (10,000 / 0.8 x 20%). The full dividend of EUR 10,000 will be paid to the shareholder, suffering no Latvian PIT.

Lithuanian tax residents

Lithuanian residents are subject to PIT at a flat rate of 15% on their worldwide income (with certain exceptions). Although Lithuania has adopted progressive taxation effective from 2019, the rate of PIT on income from distributed profits remains unchanged regardless of its amount, resulting in a more favourable taxation regime than what applies on other income.

Although the Latvia-Lithuania tax treaty allows Latvia to tax dividends a Latvian company distributes to a Lithuanian-resident taxpayer, thereby avoiding double taxation in Lithuania, the national rules should be considered in determining the final tax burden.

Under Lithuanian law, only foreign PIT (or equivalent tax) actually paid can be credited against the Lithuanian PIT liability, subject to a 15% cap. Given the Latvian PIT dividend exemption rules, the Lithuanian-resident shareholder is still subject to a 15% PIT on the gross dividend (10,000 x 15% = 1,500) because no other foreign tax, such as CIT, can be used for a PIT credit in Lithuania.

The combined tax burden on the company and the individual is a 25% CIT plus a 15% PIT payable in Lithuania on distributed profits. The dividend of EUR 10,000 paid by the Latvian company first attracts Latvian CIT of EUR 2,500 and then Lithuanian PIT of EUR 1,500, resulting in a total tax charge of EUR 4,000.

Estonian tax residents

Estonian tax-resident individuals are taxed on their worldwide income from all sources.

A tax credit is generally allowed on the foreign income tax paid by the individual. However, the tax credit is limited to the Estonian tax (flat 20%) levied on the same income. Excess foreign tax credits cannot be carried forward.

A foreign dividend distributed to an Estonian tax resident is generally exempt if the underlying profit has been subject to foreign income tax or if income tax on the dividend has been withheld under a procedure similar to the Latvian tax system.

Estonian tax law contains a general anti-avoidance rule aimed at ignoring any transaction or chain of transactions carried out primarily for the purpose of obtaining an income tax advantage.

In our example, the dividend of EUR 10,000 attracts Latvian CIT of EUR 2,500 and there is no PIT to pay by the Estonian resident.

Although foreign dividends may be exempt in Estonia, for information purposes such income should be reported on the Estonian resident's annual tax return, which is normally due by 30 April in the following year.

The individual should be able to provide the Estonian tax authority with evidence that Latvian CIT has been paid on the underlying profit (a certificate issued by the Latvian company is sufficient).

Key takeaways

Since Latvia and Estonia operate similar CIT systems after 2017, the tax burden may be eased by exempting Latvian dividends in the hands of Latvian or Estonian residents. The Latvian CIT levy is final, with no PIT due.

However, for a resident of Lithuania (or any other country operating the traditional CIT system), the absence of Latvian PIT (replaced by a higher CIT after 2017) means another tax payable in Lithuania, resulting in a higher tax burden than that borne by Latvian or Estonian residents.

This article was written in collaboration with PwC Lithuania and PwC Estonia tax teams, based on tax legislation and practice in force at the time of writing.