

Tax & Legal Alert

Lithuania • Issue 116, 16 November 2009

Tax & Legal Alert

provides the latest information on changes in Lithuanian legislation most urgent to our clients.

In this issue:

- Intrastat thresholds for 2010
- Supplement to the Commentary on the Law on CIT
- Amendments to the rules on submission of notifications 1-SD and 2-SD
- Other news



Tax news

Contacts:

Kristina Kriščiūnaitė
Partner, Head of Tax Department
E-mail:
kristina.krisciunaite@lt.pwc.com
Tel: +370 5 239 23 00

Nerijus Nedzinskas
E-mail:
nerijus.nedzinskas@lt.pwc.com
Tel: +370 5 239 23 50

Egidijus Kundelis
E-mail:
egidijus.kundelis@lt.pwc.com
Tel: +370 5 239 23 57

Daiva Šoliūnaitė
E-mail:
daiva.soliunaite@lt.pwc.com
Tel: +370 5 239 23 09

PricewaterhouseCoopers, UAB
J. Jasinskio 16B, Vilnius
Tel: +370 5 239 23 00

www.pwc.com/lt

This Tax & Legal Alert is produced by
PricewaterhouseCoopers' Tax department.

Intrastat thresholds for 2010

By Order No. [DJ-248](#) of the Head of the Department of Statistics under the Government of the Republic of Lithuania dated 29 October 2009, Intrastat thresholds for 2010 were set.

From 1 January 2010 to 31 December 2010 the Intrastat exemption threshold is as follows:

- arrivals – LTL 450 thousand (currently LTL 500 thousand);
- dispatches – LTL 500 thousand (currently LTL 650 thousand).

From 1 January 2009 to 31 December 2010 the Intrastat statistical value threshold is as follows:

- arrivals – LTL 8 million (currently LTL 10 million);
- dispatches – LTL 24 million (currently LTL 25 million).

Amendments to the Commentary on the Law on CIT

On 7 October 2009 by letter No. [\(18.10-31-1\)-R-9606](#) the Tax Authorities informed that the Commentary on art. 21 part 3 of the Law on CIT was supplemented.

Apart from editorial amendments, the Commentary was updated due to the changes in calculation of daily allowances for a business trip inside Lithuania applicable from March 2009.

The Commentary was supplemented by the example describing how daily allowances for a business trip inside Lithuania are calculated based on the basic social allowance which is currently LTL 130.

The Commentary was also supplemented by the explanation regarding deduction of business trip expenses in cases when a special negotiation committee member but not an employee is sent on a business trip.

On 13 October 2009 by letter No. [\(18.10-31-1\)-R-9842](#) the Tax Authorities informed that the Commentary on art. 26 of the Law on CIT was supplemented. The supplement provides that voluntary premiums for accident and (or) health insurance paid on behalf of employees based on a life insurance contract are regarded as life insurance premiums.

It means that such premiums are also regarded as limited allowable deductions which can be enjoyed if other requirements of the Law are met.

On 16 October 2009 by letter No. [\(18.9-31-1\)-R-9966](#) the Tax Authorities informed that the Commentary on art. 17 part 1 of the Law on CIT was supplemented.

The Commentary was supplemented by an explanation according to which costs on animals dead due to a disease, injury or malformation, as well as costs on agricultural products which cannot be

sold due to animal disease can be deducted for CIT purposes.

The Commentary specifies the documents which are required in such cases. It also explains that costs of dead animals and costs of agricultural products unsold cannot be deducted if an insurance compensation fully covering such losses is received.

Amendments to the rules on submission of notifications 1-SD and 2-SD

On 29 October 2009 by Order of the Managing Board of the State Social Insurance Fund No. [V-634](#) the rules on submission of the notification about the start of social insurance coverage for insured persons 1-SD and the notification about the end of social insurance coverage for insured persons 2-SD were amended.

The amendments provide that these notifications shall be submitted only via the electronic service centre.

The possibility to submit these notifications by fax or by post office is provided only for those entities which have 9 or less persons employed.

Moreover, the notification 2-SD includes a requirement to refer to the particular legislation based on which an employee is dismissed as well as to provide additional information on the amount of compensation paid, i.e. it must be indicated for how many months the compensation was calculated.

These new requirements will come into effect on 1 December 2009.

Amendments to the rules on ordering and issuing of excise duty stickers for processed tobacco, ethanol and alcohol

On 20 October 2009 by Order No. [VA-67](#) of the Head of the Tax Authorities rules on ordering and issuing of excise duty stickers for processed tobacco, ethanol and alcohol were amended.

According to the amendments, from 1 May 2009 a request for production of excise duty stickers for the respective month should be provided to the Tax Authorities before 15th day of the month (previously this was required to be done before 5th day of the month).

The Tax Authorities will be obliged to submit a summary of such requests to the excise duty stickers printing-house not later than on the 20th day of the subsequent month (previously not later than on the 10th day of the subsequent month).

News from the EU

On 31 November 2009 the European Commission published a new [version](#) of the Combined Nomenclature for 2010, which should be applicable from 1 January 2010.

Draft legislation

Law on CIT

On 16 October 2009 draft amendments to the Law on CIT No. [XIP-1222](#) and [XIP-1223](#) were registered with the Lithuanian Parliament.

According to the draft amendments, the following is suggested:

- reduction of standard CIT rate from 20% to 15%, from 13% to 7.5% for small entities with a number of employees not exceeding 10 and taxable income not exceeding EUR 144,810;
- WHT should be reduced respectively (from 20% to 15%) for income received by non-resident companies;
- income received by a Lithuanian company through a permanent establishment in EEA Member States or in a country with which a double taxation treaty is signed should not be attributed to the taxable base of this company provided that CIT or similar tax was applied to such income in the foreign country;
- amendments to the rules on deductibility of expenses for the benefit of employees or their family members;

- dividends which qualify for participation exemption requirements should not be taxable irrespective of any CIT incentives applied to the profit distributed. The restrictions enacted from 1 January 2009 should be abolished;
- a possibility to attribute long-term assets which are registered with respective registers to certain group of assets only in accordance to their actual purpose;
- possibilities to transfer losses between group entities.

If the draft legislation is enacted, most of the aforementioned amendments would come into force and would be applicable from 1 January 2010.

Law on Tax Administration

On 10 October 2009 the Lithuanian Ministry of Finance prepared draft amendments No. [2129-01](#) to the Lithuanian Law on Tax Administration. According to the draft amendments, companies will have a possibility to obtain binding rulings from the Lithuanian Tax Authorities for application of certain provisions of tax legislation for future transactions.

Draft amendments also provide for a possibility to apply to the Tax Authorities with a request for Advance Pricing Agreement establishing transfer pricing principles applicable to transactions with related parties.

The aforementioned provisions would be applicable from 1 January 2011.

We would like to draw your attention to the fact that such possibilities are widely used in many countries of the world. If such amendments are enacted, individual situations of tax payers would be analysed separately and an individual approach would be applied. However, other clauses of the draft legislation should be taken into consideration, e.g. a binding ruling would be repealed if the provisions of the legislation supporting this ruling are amended, as well as other conditions.

On 22 October 2009 draft amendments No. [XIP-1297](#) to the Law on Tax Administration were registered with the Lithuanian Parliament.

The draft amendments suggest restrictions of the procedures of tax inspection and investigation performed by the Tax Authorities. According to the draft amendments the period of their performance as well as extension of the periods should be reduced. It is also suggested that the Tax Authorities are not allowed performing the same actions during a tax investigation as they are performed during a tax inspection.

The aforementioned amendments would be favourable for entities as this would prevent delays in completion of tax investigations or tax inspections, make the process more efficient as well as reduce the disturbance of activities of the tax payer.

Draft Commentary of the Law on CIT

In October 2009 the Tax Authorities prepared draft Commentaries of art. 2 and 17(1) of the Law on CIT. These commentaries are currently under discussion and will be published shortly.

The draft commentary explains and provides for practical examples on how R&D relief introduced in 2008 should be applicable by companies involved in R&D activities.

News from the Tax Authorities

Regarding terminated lease agreements

On 22 October 2009 the Tax Authorities published a [notification](#), where remind that upon a termination of a lease agreement, a lessee returning the leased assets to a lessor is also liable to adjust (reduce) VAT deduction based on a credit note received.

Practice of the Tax Authorities

On 27 October 2009 an [interview](#) with the Head of Controls Department of the Tax Authorities Artūras Klerauskas was published on Infolex.lt.

According to the interview, due to the economy downturn, for the purpose of avoidance of fraud and tax evasion, the control of tax payers will be increased.

The most attention will be paid to the following:

- payments in cash between entities and individuals;
- control of loss-making activities;
- export to Member States with zero-rated VAT;
- transactions with offshore territories;
- major tax payers;
- transactions between group companies;
- administration of payments overdue for the purpose of anticipation of possible business redeployment.

We would like to draw your attention to the fact that the Tax Authorities are currently paying increased attention to activities of foreign companies in Lithuania and evaluate possible permanent establishment creation risk.

Increased attention is also paid to companies performing transactions with related parties, i.e. the Tax Authorities request for providing Transfer Pricing documentation for review more frequently. Benchmarking studies and their results are being checked with high intention.

Legal news

Model Regulations of a Personal Company have been adopted

On 19 October 2009 Order of the Minister of Economics of the Republic of Lithuania No. [4-525](#) approved model regulations of a personal company. The same order also adopted recommendations regarding completion of the mentioned regulations. From now on persons who would like to establish a personal company will be able to use the model regulations, therefore, the whole process of the establishment of a personal company will become less complicated. In addition, extra money and time will also be saved.

New rate of the maximum technical interest approved

On 6 October 2009 Order of the Insurance Supervisory Commission of the Republic of Lithuania No. [N-444](#) approved a new rate of the maximum technical interest which now will be equal to 2.38 %.

Draft legislation

Lithuanian Government proposes to simplify regulation of companies

The draft amendments No. [323-02](#) to the Lithuanian Law on Companies which have already been approved by the Lithuanian Government foresees many important changes. The purpose of proposed changes is to provide more freedom for private limited liability companies to organize their activities and to accelerate the incorporation process. Moreover, the draft legislation also includes suggestions to decrease the amount of the obligatory share capital of a private limited liability company from LTL 10 000 to LTL 1 000 and to withdraw the requirement for such companies to limit the maximum number of shareholders to 249.

The draft legislation also foresees a possibility for companies to announce their public information by electronic means of communication and withdraws the obligation to convene the constitutive meeting of the shareholders. The draft legislation also includes

a possibility to conclude a civil agreement with the general manager of the company and to foresee his resignation order. Moreover, the draft legislation establishes new requirements for companies. According to the provisions of the draft Law, companies would be obliged to compose a list of all shareholders and submit it to the Lithuanian Register of Legal Entities.

The draft legislation also foresees other provisions and requirements. All of these provisions should help solving practical problems and upgrade the whole business environment.

Tax case-law

Requalification of the disposal of shares into dividends received

On 28 September 2009 the Supreme Administrative Court of Lithuania (SACL) decided in the administrative case No. [A-556-1034/2009](#). The case examined whether the Tax Authorities legitimately, based on the substance over form principle, requalified an income from the disposal of shares into dividends received.

In the case it was established that an individual shareholder of a Lithuanian company (hereinafter – the Company) sold all of his shares in the Company to an Estonian entity. Based on the Law on Personal Income Tax, the capital gains on the disposal of these shares were not subject to personal income tax.

After the above mentioned disposal of shares was completed, the Company distributed dividends to the Estonian entity. The amount of dividends distributed slightly varied from the capital gains on the disposal of shares received by the former Company's shareholder. Based on the Law on CIT, the dividends concerned were not subject to WHT.

Shortly after the above-mentioned transactions were completed, the Company's activities were ceased and subsequently its liquidation procedures were launched.

Moreover, during the tax investigation the Tax Authorities established that the founder of the above-mentioned Estonian entity is a non-existing entity.

Based on the above, the Tax Authorities decided that the above-mentioned transactions do not meet the actual business needs and they are concluded formally with a view of gaining a tax benefit. Therefore, based on the substance over form principle, the capital gains on the disposal of shares received by the individual shareholder were requalified into dividends received from the Company. As a result, additional personal income tax was calculated on these dividends for the Company as a tax withholding agent.

SACL in its decision stated that based on all relevant circumstances in the case it can be concluded that before the disposal of shares the Company's individual shareholder clearly realized the state and perspectives of the Company. Therefore, the model of the sale of shares to the Estonian entity and subsequent distribution of dividends was chosen, thus avoiding taxes due. SACL also emphasized that no reliable and sufficient evidence were gathered in the case proving that other than a tax benefit was pursued in the course of the above-mentioned transactions.

Based therein, the Company's appeal regarding additional PIT was rejected.

Please note that the recent tax case-law shows that the Tax Authorities pay exclusive attention to the actual substance of a transaction. If it is determined by the Tax Authorities that a particular transaction is concluded only with a view of gaining a tax benefit, the substance over form principle is applied and additional taxes are calculated.

ECJ: Sale of portfolio of (re)insurance contracts is VAT taxable

On 22 October 2009 the European Court of Justice (ECJ) handed its decision in Case [C-242/08](#) (*Swiss Re*).

It concerns the situation where a German insurance company transferred 195 reinsurance contracts to an associated Swiss insurance company (with a negative value). The recipient obtained all rights and obligations arising from the contracts.

The German Tax Authorities treated this transaction as a supply of goods taxable with local VAT. *Swiss Re* disputed such treatment and attempted to prove that the transaction should be VAT-exempt. The German court ruled that the transaction should be treated as supply of services taxable with German VAT which is non-recoverable for the purchaser of the contracts that will be engaged in VAT-exempt insurance services in relation to the contracts acquired.

ECJ decision:

- the sale of a portfolio of contracts should be regarded as supply of services (not supply of goods);
- the sale of a portfolio of (re)insurance contracts is not treated as VAT-exempt service.

Implications

Although ECJ did not analyse whether or not such a sale of portfolio of contracts could be treated as a transfer of a going concern, such treatment of the transaction cannot be excluded. Transfer of a going concern (or as per commentary on the VAT Law - 'a sale of a business as a complex') is treated as a supply of goods in Lithuania. When a business is sold by a taxable person supplying financial services that does not enjoy VAT deduction, such a supply is VAT-exempt.

However, due to the decision of the ECJ in Case C-242/08 attention should be drawn to the risk that where the Lithuanian Tax Authorities decide that a sale of a portfolio of contracts examined by them does not meet the requirements for a 'sale of a business as a complex', the transaction would be re-qualified to a VAT taxable supply of services. This is especially important to taxable persons which cannot deduct any input VAT.

ECJ: Possibility to deduct input VAT incurred on sale of shares in a subsidiary

On 29 October 2009 ECJ handed its decision in Case [C-29/08](#) (*AB SKF*).

It concerns a case where the Swedish company AB SKF intended to dispose of the shares in its subsidiary and 26.5% of shares in another controlled company. AB SKF rendered VAT taxable management and other services to both of these companies. Taking into account possible input VAT costs, AB SKF applied to a Swedish court for a preliminary ruling on whether input VAT related to sale of the shares could be deductible, and they received a positive ruling. However, this ruling was disputed by the Swedish Tax Authorities.

ECJ decision:

- the sale of shares is subject to VAT, i.e. constituting economic activities;
- the sale of shares is exempt from VAT;
- input VAT related to sale of shares is not deductible, unless this input VAT constitutes a part of the general expenditure required for economic activities of SKF – in such a case input VAT could be deductible in accordance to SKF VAT recovery position;
- the sale of shares can be treated as a transfer of a going concern.

Implications

According to the generally accepted opinion on VAT deductions and practice applied, such input VAT is treated as non-deductible. However, on the basis of the ECJ ruling in this Case, any company that sold its shares held in controlled companies and that was actively involved in their management could seek to prove that input VAT incurred in relation to the sale of the shares constitutes a part of the general expenses required for economic activities and thus it could be treated as deductible. Moreover, if a particular sale of shares could be regarded as a transfer of a going concern – the rule which as from 1 January 2010 will be implemented in Lithuania resulting in treatment of a transfer of a 'business as a complex' as being out of scope of VAT – there could be a possibility for deduction of such input VAT.

Tax & Legal Alert

Lithuania • 16 November 2009

Legal Disclaimer: The material contained in this alert is provided for general information purposes only and does not contain a comprehensive analysis of each item described. Before taking (or not taking) any action, readers should seek professional advice specific to their situation. No liability is accepted for acts or omissions taken in reliance upon the contents of this alert.

© 2009 PricewaterhouseCoopers UAB. All rights reserved. "PricewaterhouseCoopers" refers to the Lithuania's firm of PricewaterhouseCoopers UAB or, as the context requires, the network of member firms of PricewaterhouseCoopers International Limited, each of which is a separate and independent legal entity.