

International transfer pricing 2009

Lithuania



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4501 Introduction

The arm's length principle was only introduced in Lithuania by the Corporate Tax Act of 20 December 2001. Little attention was paid to transfer pricing before this time. The OECD Transfer Pricing Guidelines have been carried over into Lithuania's domestic transfer pricing legislation, although in a more condensed form, and with a somewhat clearer stance on a number of questions.

4502 Statutory rules

The definition of related parties includes, inter alia, a) members of a group consisting of a parent and one or more of its 25% or greater subsidiaries, b) two entities if one of them directly or indirectly controls over 25% of the shares in the other entity, or has the right to over 25% of voting rights of the other entity, or has an obligation to coordinate its business decisions with that entity, or is under an obligation to third parties for the obligations the entity c) two entities where one has the right to make decisions that bind the other. The term 'associated parties' to which transfer pricing rules also apply, covers all entities which may influence each other as a result of which conditions in transactions between them differ from those which would occur if each entity were acting to maximise its own profit (i.e. there is no requirement to have shareholding or voting ties).

4503 Other regulations

In 2007, the Tax Authorities issued official recommendations on transfer pricing "For tax payers about transfer pricing". These recommendations are based on the OECD Transfer Pricing Guidelines.

4504 Legal cases

There are no prior court cases relating to transfer pricing.

4505 Burden of proof

By law, the tax authority needs to make a case for an adjustment. In practice, however, it is often the case that a comparatively simple opening argument results in the taxpayer having to make substantial effort to build a defensive case.

4506 Tax audit procedures

Tax audits are more likely following a refund claim, a tip-off or liquidation. There are two types of procedures – limited and full. Either procedure can cover either a specific tax or the whole range of taxes. There is a standard 90 day time limit on the duration of any investigation, although this can be extended. There is a five year statute of limitations.

4507 Revised assessments and the appeals procedure

The appeals process is firstly to the officer conducting the investigation, then to a more senior person at the tax office, followed by the commission for tax disputes and finally the courts. In practice, however, most disputes over reasonably grounded differences in interpretation are settled in comprise without litigation.

4508 Additional tax and penalties

There is a misdeclaration penalty of between 10% and 50% of the tax, the exact amount being discretionary. A penalty may be limited if there is no overall loss to the state budget, for example through a corresponding adjustment. In addition, there would be penalty interest calculated as 0.04% of the unpaid tax per day.

4509 Resources available to the tax authorities

There are only three persons specialising solely in transfer pricing within the tax authorities. This indicates that the authorities are not as experienced as many other EU tax authorities. There have been comparatively few public statements, or high profile investigations to date. However, recently they have started requesting the companies to submit the transfer pricing documentations for review within a 30 days (statutory) period.

4510 Use and availability of comparable information

The authorities already have direct access to the Amadeus database. They focus on adjustments to internal comparable uncontrolled prices, including analysis of margins and mark-ups on transactions between the taxpayer and unrelated parties. However, they are already reviewing the benchmarking studies as well. Lithuania is not an OECD member and local rules allow the use of secret comparables in certain cases.

4511 Risk transactions or industries

At present the most notable risk transactions are those involving various types of services or management fees. There are a number of benefit tests and emphasis placed on demonstrating the actual performance of a service.

4512 Limitation of double taxation and competent authority proceedings

Competent authority proceedings have not yet been frequently requested by taxpayers.

4513 Advance pricing agreements (APAs)

There is a tax ruling procedure which can be used to avoid penalties, and the system is in general sufficiently flexible to cover many aspects of transfer pricing. Currently the tax rulings are not binding and the tax authorities usually try not to provide detailed answers to the questions. However work continues at the level of the Ministry to set up the framework for a more formal APA system.

4514 Anticipated developments in law and practice

At present there are no penalties for failure to comply with documentation rules, but

it is possible that this may change. Furthermore, the appendix to the corporate tax return in which related party balances should be disclosed is expected to become clearer. At present there is uncertainty over precisely what information is being requested.

4515 Liaison with customs authorities

There is minimal interaction between inspectors responsible for direct tax and their colleagues in customs.

4516 OECD issues

Lithuania is not an OECD member but follows the organisation's guidelines closely with respect to interpretation of double tax treaties. However for transfer pricing, local rules take precedent, in the event of conflict with the OECD Guidelines. One example is the use of secret comparables, which is permitted by local legislation in certain cases.

4517 Joint investigations

At present, the Lithuanian authorities are not making extensive use of exchange of information opportunities.

4518 Thin capitalisation

Very broadly, interest on debt exceeding a 4:1 debt-equity ratio is disallowed (unless it can be proven that an unrelated party would have lent at higher gearing). Debt from persons who on their own or together with related parties own directly or indirectly 50% of the payer is considered. For the purposes of the calculation, year-end balances are used (unless the tax authorities deem these unrepresentative), and the definition of equity is the balance on the last day of the tax period, excluding the financial result of the period and certain revaluation reserves. Interest from unrelated banks is not subject to thin capitalisation restrictions, unless an associated enterprise guarantees the debt.

4519 Management services

Management services fall under particular scrutiny as historically, over the past 15 years, they have been seen by investors as simply a repatriation tool which does not require the legal procedures of a dividend and also offers a tax deduction. Tax authorities lacked the resources and commitment to challenge this practice effectively. For this reason, shared service centres and headquarters are facing increased documentation burdens and Lithuanian finance personnel are increasingly reluctant to take responsibility for the effects of any such charge, sometimes even adding it back for tax purposes regardless of substance.

The law specifically states that taxpayers should demonstrate that services were actually rendered, normally meaning objective tangible evidence such as reports or travel documents. There is also a benefit test, which appears to be an either/or rather than a cost to benefit comparison. Duplication of services is not permitted, which may inadvertently lead to difficulties in services which support or build on existing resources. Also of note is the non-deductibility of costs related to services which are

deemed to arise from merely being a participant in a group, possibly referring to the benefits of centralised purchasing and similar functions, although there is yet little practical experience of how this rule will be applied.

Transfer pricing considerations affect every company, large or small, with international affiliates, offering planning opportunities whilst imposing increasingly burdensome compliance obligations. As governments throughout the world implement stringent transfer pricing regulations, those multinationals without a robust, consistent and defensible policy will be exposed to financial penalties exacted by fiscal authorities.

International Transfer Pricing 2009, now in its eleventh edition, provides companies and their advisors with practical guidance on how to approach the issue of determining defensible transfer pricing across the full range of goods and services, as well as how to prepare for the negotiations in which they must be sustained. This edition has been updated to include fully revised overviews of the position in sixty countries, seeking to provide clear and comprehensive coverage of this complex subject.

The book has been written in the light of extensive knowledge and experience gathered by the global transfer pricing network of PricewaterhouseCoopers. The principal author and editor of the 2009 edition is Nick Raby, transfer pricing principal and leader of the PricewaterhouseCoopers practice in the Western United States.

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