FOREWORD

A country's tax regime is always a key factor for any business considering moving into new markets. What is the corporate tax rate? Are there any incentives for overseas businesses? Are there double tax treaties in place? How will foreign source income be taxed?

Since 1994, the PKF network of independent member firms, administered by PKF International Limited, has produced the PKF Worldwide Tax Guide (WWTG) to provide international businesses with the answers to these key tax questions.

As you will appreciate, the production of the WWTG is a huge team effort and we would like to thank all tax experts within PKF member firms who gave up their time to contribute the vital information on their country's taxes that forms the heart of this publication.

The PKF Worldwide Tax Guide 2016/17 (WWTG) is an annual publication that provides an overview of the taxation and business regulation regimes of the world's most significant trading countries. In compiling this publication, member firms of the PKF network have based their summaries on information current on 30 April 2016, while also noting imminent changes where necessary.

On a country-by-country basis, each summary such as this one, addresses the major taxes applicable to business; how taxable income is determined; sundry other related taxation and business issues; and the country's personal tax regime. The final section of each country summary sets out the Double Tax Treaty and Non-Treaty rates of tax withholding relating to the payment of dividends, interest, royalties and other related payments.

While the WWTG should not to be regarded as offering a complete explanation of the taxation issues in each country, we hope readers will use the publication as their first point of reference and then use the services of their local PKF member firm to provide specific information and advice.

Services provided by member firms include:

- Assurance & Advisory;
- Financial Planning / Wealth Management;
- Corporate Finance;
- Management Consultancy;
- IT Consultancy;
- Insolvency - Corporate and Personal;
- Taxation;
- Forensic Accounting; and,
- Hotel Consultancy.

In addition to the printed version of the WWTG, individual country taxation guides such as this are available in PDF format which can be downloaded from the PKF website at www.pkf.com
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I. TREATY AND NON-TREATY WITHHOLDING TAX RATES
MEMBER FIRM

City | Name | Contact Information
--- | --- | ---
Riga | Maruta Zorgenfreija | +371 67 333 647
 |  | maruta.zorgenfreija@pkf-latvia.lv

BASIC FACTS

Full name: Republic of Latvia
Capital: Riga
Main languages: Latvian, Russian
Population: 2 million (2013 PRB)
Major religion: Christianity
Monetary unit: Euro (EUR)
Internet domain: .lv
Int. dialling code: +371

KEY TAX POINTS

- Resident taxpayers are subject to corporate income tax on their worldwide income. Foreign entities are subject to tax on income earned in Latvia. Branches of foreign entities are subject to tax on worldwide income attributable to the branch. Corporate income tax rate is 15%.
- Capital gains of companies are treated as ordinary income and taxed accordingly unless specifically exempt.
- The general rate of VAT is 21%. A reduced rate of 12% is applied to certain products and services. Intra Community supply of goods (to a customer registered as a VAT payer in another Member State) is zero-rated.
- Foreign income tax suffered at source may be credited against the corporate income tax charge calculated for a taxation year.
- In respect of related party transactions, when determining taxable profit, accounting profit shall be increased for the difference between market price and transaction price if goods, fixed assets, services are sold/purchased to/from non-resident related parties or resident related parties enjoying tax holidays, or companies within the tax group, or related persons.
- Withholding tax is levied at standard rates on certain payments made by Latvian residents to non-residents. If a double tax treaty exists between Latvia and the relevant country, reduced rates or exemptions may be applied.
- In 2016, Latvian residents are liable to personal income tax at a flat rate of 23% on their worldwide income. Non-residents are liable to personal income tax at a flat rate of 23% on their Latvian source income.

A. TAXES PAYABLE

COMPANY TAX

A company is resident in Latvia if it is registered, or required to be registered, in Latvia. Resident taxpayers are subject to corporate income tax on their worldwide income. Foreign entities are subject to tax on income earned in Latvia. Branches of foreign entities are subject to tax on worldwide income attributable to the branch.

Companies may choose the accounting and taxation period which does not necessarily have to be the calendar year and the length of the taxation (accounting) period is 12 months. Only the first accounting period can be longer than 12 months (subject to a maximum of 18 months). Taxable income is based on accounting profit which is adjusted according to the provisions of the Corporate Income Tax Act. Tax is charged on profits at the rate of 15%. Companies are required to make advance payments of tax based on the prior year tax amount. Shipping companies may alternatively apply tonnage tax.
CAPITAL GAINS TAX

Capital gains are treated as ordinary income and taxed accordingly, unless specifically exempt (see capital gains and losses).

BRANCH PROFITS TAX

Branch offices are treated as domestic companies. Branches of foreign entities are subject to tax on worldwide income attributable to the branch.

VALUE ADDED TAX (VAT)

The general rate of VAT is 21%. A reduced rate of 12% is applied to certain products and services such as medical goods (according to the list approved by the Cabinet of Ministers), baby food, supplies of books, mass media, inland public transportation services, hotel services (accommodation) and supplies to individuals of heating. Exports and related services are zero-rated. Several types of supplies are VAT exempt. These include sale of land (except development land with building permission issued after 31 December 2009) and used real estate; supply of medical services; rental of apartments to individuals; and most banking and insurance services. Intra-Community supply of goods (to a customer registered as a VAT payer in another Member State) is zero-rated.

A transaction that involves a Latvian taxable person acquiring goods in Latvia from a taxable person registered in another Member State will qualify as an intra-Community acquisition within the meaning of the VAT Act. When the Latvian taxable person receives the goods from a supplier, this person will charge VAT on the acquisition and will recover this amount as input tax in the same month (reverse charge accounting). The VAT registration threshold is EUR 50,000. There is a 50% restriction on deducting input tax on light passenger cars that are purchased, rented or imported and on their running costs including fuel and repairs (except where the car is used for passenger and carrying goods, taxi services, lease services, and some other specialised services). VAT is not deductible on representative cars (cost exceeding EUR 50,000).

Reverse charge accounting applies to construction services supplied in Latvia. VAT is to be calculated by a customer rather than a supplier of construction services (both VAT payers in Latvia); the customer pays the supplier without VAT, and calculates and shows VAT as input and output tax (if services have been acquired to make taxable supplies). The VAT Act provides a list of construction services to which reverse charge accounting applies (such as preparing a construction site, construction of supporting and non-supporting elements or structures for a building, internal decoration etc.). From 1 April 2016 reverse charge VAT applies to supplies of smartphones, laptops, tablets, and integrated circuit devices (including microprocessors and central processing units).

FRINGE BENEFITS TAX

Most fringe benefits granted to employees are subject to payroll taxes. A few benefits are tax exempt. These include health and accident insurance premiums paid on agreements concluded by employers on behalf of their employees; and contributions to private pension funds or life insurance premiums on the employee's behalf. Health and life insurance premiums and contributions to private pension plans that are no higher than 10% of gross remuneration of an employee in the taxation year are not subject to payroll taxes. Certain conditions need to be met and health and accident insurance premiums may not exceed EUR 426.86.

LOCAL TAXES

Local authorities are permitted to levy stamp duties. They may be levied on transactions such as obtaining a building permit; placements of advertisements at public locations; organising public trading events, etc.
REAL ESTATE TAX

Real estate tax is paid by Latvian and foreign companies and individuals that have title (registered with the Land Registry) or legal possession of real estate in Latvia i.e. land, buildings and engineering structures - roads, bridges, pipelines, communication lines, power station structures, fencing, etc. The standard rate of real estate tax applicable to land, buildings (except residential buildings) and constructions is 1.5% of cadastral value. The local authorities have the right to set the rate of real estate tax within a range of 0.2 - 3%. If the local authority fails to announce a different rate by 1 October for the following year, the standard rate of 1.5% will apply for that following year.

From 2014 the local authorities, when issuing binding regulations, have rights to apply 3% tax rate for buildings that exceed certain construction works’ duration, starting from the next month after the construction term expires till the month when the building acceptance document is signed. Tax is calculated on the cadastral value of land, buildings and engineering structures. Some classes of real estate are exempt of tax such as state or municipal real estate used for performing certain functions. A progressive rate has been set for residential houses and any parts of non-residential buildings that are functionally used for living and not used in a trade or business:

- 0.2% of cadastral values up to EUR 56,915;
- 0.4% of cadastral values exceeding EUR 56,915, but not exceeding EUR 106,715;
- 0.6% of cadastral values exceeding EUR 106,715.

A double rate of 3% (standard rate 1.5% plus additional rate 1.5%) applies to uncultivated land capable of agricultural use. If such property, in addition, is not maintained in accordance with regulatory requirements, the local authority can set a rate of up to 4.5% consisting of maximum allowable rate 3% plus additional rate 1.5% for uncultivated land.

OTHER TAXES

Stamp Duty is payable on registration of title to real estate with the Land Book at 2% of purchase price (or cadastral value if higher), up to a maximum of EUR 42,686.

B. DETERMINATION OF TAXABLE INCOME

Taxable income includes income from all activities of the company and capital gains. The accounting profit before tax (as per the income statement) is adjusted in accordance with the corporate income tax rules.

DEPRECIATION

For tax purposes, tangible fixed assets used in a business should be depreciated using the reduced balance method. The rates are as follows:

<table>
<thead>
<tr>
<th>Type of Assets</th>
<th>Rate (%)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Buildings, structures and perennial plantings</td>
<td>10</td>
</tr>
<tr>
<td>Technology and energy installations, fleet, railway</td>
<td>20</td>
</tr>
<tr>
<td>Computer hardware and software</td>
<td>70</td>
</tr>
<tr>
<td>Oil exploration and extraction platforms</td>
<td>15</td>
</tr>
<tr>
<td>Aircraft, light motor vehicles in general</td>
<td>30</td>
</tr>
<tr>
<td>Other fixed assets</td>
<td>40</td>
</tr>
</tbody>
</table>

There is an incentive for the acquisition of new production technological equipment. For tax depreciation purposes, the amount to be depreciated is the cost of equipment multiplied by a
The coefficient to be applied in respect of equipment acquired in 2014-2020 is 1.5. Such equipment may not be sold within the next five years from acquisition in order to benefit from the enhanced allowances.

No capital allowances are available on investment property accounted for at fair value. Representative vehicles (cars) worth (which cost) more than EUR 50,000 excluding VAT may not be depreciated for tax purposes and all costs associated with their usage and maintenance shall be treated as non-deductible expenses for income tax purposes. Intangible assets should be depreciated on a straight-line basis over the following period:

<table>
<thead>
<tr>
<th>Type of Intangible Asset</th>
<th>Years</th>
</tr>
</thead>
<tbody>
<tr>
<td>Concessions</td>
<td>10</td>
</tr>
<tr>
<td>Patents, licences and trademarks</td>
<td>5</td>
</tr>
<tr>
<td>Research and development costs</td>
<td>1</td>
</tr>
</tbody>
</table>

Any other intangible assets, which are not included in the above categories, cannot be depreciated for tax purposes.

**STOCK / INVENTORY**

Inventories are generally valued at the lower of cost and market value. Cost may be determined on the basis of FIFO or weighted average cost (as per accounting rules). Unrealised loss (amount of write-down to market value) is not deductible for income tax purposes.

**CAPITAL GAINS AND LOSSES**

The amendments to the Corporate Income Tax (CIT) Act which took effect on 1 January 2013 include provisions that should make Latvia a more attractive country for holding companies. From 2013, income from the disposal of shares is exempt from CIT. This exemption does not apply to a gain on the sale of shares of companies located in tax haven countries. Losses from sale of shares are not deductible for CIT purposes. Other capital gains, in general, are taxed as ordinary income (at 15%).

Payment of tax on profits arising on the sale of an asset may be deferred if the company acquires a functionally similar asset within 12 months before or after the old equipment is disposed of. The gain is rolled over into the base cost of the new asset and becomes chargeable when the new equipment is sold. This provision does not apply to works of art, antiques, jewellery, investment properties, long term investments held for sale; motorcycles, watercraft, aircraft, and light passenger vehicles. Capital losses on other assets are deductible from ordinary income. Interest from public debt securities of issuers from EU and EEA countries is tax exempt.

**DIVIDENDS**

Dividend income received by a Latvian company is tax exempt. Only dividends received from tax havens attract CIT (at 15%). Dividends paid by Latvian companies to non-resident companies (other than those registered in tax havens) are exempt from withholding tax.

In 2014 a new concept of extraordinary dividends was introduced in the Commercial Law. According to the Commercial Law, the companies are allowed to include in its Articles of Association a provision allowing to pay interim (extraordinary) dividends based on profit earned in the period from the last day of the previous year to the end of the interim period. There are special rules set by law which the company has to comply with in order to pay interim dividends; the amount of the dividend should not exceed 85% of the interim profit, the interim accounts should be prepared and the company must not have tax debts at the moment of making dividend decision and some others.
INTEREST DEDUCTIONS

There are thin capitalisation rules for interest deductions. Interest charges exceeding statutory limits are not deductible for tax purposes. There are two restrictions on interest deduction with which the company should comply (if taxable income requires adjustments under both criteria, it should be adjusted only for the larger amount).

- Interest paid is disallowed to the extent that it exceeds the amount of the relevant loan multiplied by 1.57 times the annual weighted average rate of interest on loans issued to non-financial Latvian businesses as determined by the Bank of Latvia for the tax period;
- Taxable income should be adjusted where the associated liabilities exceed four times the shareholders’ equity at the beginning of the tax year, less any revaluation reserve and any other reserves not made as a result of profit.

The restriction does not apply to interest paid to credit institutions, including EU registered credit institutions. The following interest payments are fully deductible:

- Interest paid on borrowings from credit institutions in Latvia, other Member States, EEA member states or countries with which Latvia has an effective double tax treaty (DDT);
- Interest paid on borrowings, leases from a financial institution which:
  a) Is a resident of Latvia, EU Member State, EEA or a country with which Latvia has a DDT;
  b) Provides lending services or finance leases and is monitored by the particular country’s bodies formed to supervise credit institutions or the financial sector;
- Interest paid on debt securities in public trading.

Any amount exceeding the allowed interest for the tax period cannot be carried forward.

LOSSES

Tax losses incurred up to 2007 can generally be carried forward for eight years. Tax losses arising in 2008 and later may be carried forward indefinitely.

FOREIGN SOURCED INCOME

Tax is levied on resident companies on all profits arising from foreign sources in the same way as income from Latvian sources.

INCENTIVES

Research and development costs related to the economic activity of the taxpayer may be written off in the year in which they are incurred. Where the value of a project is not included in the value of fixed assets, research and development costs include costs related to the preparation of technical documentation. From 2014 new relief for conducting scientific and development activity has been introduced allowing to apply coefficient 3 to certain costs directly associated with this activity (e.g. employing scientific workforce, purchasing research services from specialized scientific institutions).

C. FOREIGN TAX RELIEF

Foreign income tax suffered at source may be credited against the corporate income tax charge calculated for a taxation year. Relief for tax paid abroad is available upon presentation of documents provided by the competent tax authority of the country concerned and evidencing the amount of foreign tax suffered. The amount credited is calculated for each country separately and may not exceed the Latvian tax on such income.

D. CORPORATE GROUPS

The concept of tax (corporate) group is relevant for transfer pricing as prices applied between companies in a tax group shall be in line with market prices. Direct or indirect ownership of at least 90% is a necessary condition for membership of a group. The parent must be a resident individual or
legal entity or resident in a country with which Latvia has a double tax treaty or in an EEA country. It is not allowed to transfer tax losses within a tax group.

**E. RELATED PARTY TRANSACTIONS**

In respect of related party transactions, when determining taxable profit, accounting profit shall be increased for the difference between market price and transaction price if goods, fixed assets, services are sold/purchased to/from non-resident related parties or resident related parties enjoying tax holidays, or companies within the tax group, or related persons. Adjustments may be made to reduce profits chargeable to tax where a company enters into a transaction with a related person, a related foreign company, a resident company enjoying tax holidays, or other company belonging to the same tax group and the transaction has not been entered into on arm’s length terms, provided the transaction partner has increased its taxable income.

The provision applies if the transaction partner is a Latvian resident or resident of other EU country or EEA country with which Latvia has a DTT, and if the company (tax payer) files with the State Revenue Service confirmation from the tax authorities of the other country that taxable income has been increased to reflect arm’s length pricing.

**F. WITHHOLDING TAX**

Withholding tax is levied on the following payments made by Latvian residents to non-residents.

<table>
<thead>
<tr>
<th>Description</th>
<th>Rate</th>
</tr>
</thead>
<tbody>
<tr>
<td>Dividends</td>
<td>0% (15% if payments to companies registered in tax havens; 30% - in case of payments of extraordinary dividends to tax haven entities)</td>
</tr>
<tr>
<td>Management and consulting services</td>
<td>10%</td>
</tr>
<tr>
<td>Interest payments to related companies (non-banks)</td>
<td>0%</td>
</tr>
<tr>
<td>Bank interest payments to related banks</td>
<td>0%</td>
</tr>
<tr>
<td>Copyright</td>
<td>0%</td>
</tr>
<tr>
<td>Other intellectual property</td>
<td>0%</td>
</tr>
<tr>
<td>Rental payments (in respect of property located in Latvia)</td>
<td>5% (except rent of aircraft used in international traffic, as well as payments for rights to use production, commercial or scientific equipment; for these types of payments – 0%)</td>
</tr>
<tr>
<td>Sale of real estate</td>
<td>2% of proceeds of sale (includes also income from sale of shares of companies where real estate comprises more than 50% of company’s total assets)</td>
</tr>
</tbody>
</table>

Note: All payments to companies registered in tax havens, except payments for purchases of goods and for purchases of public securities registered in EU or EEA countries, attract 15%, unless specifically agreed with the tax authorities. However, the mentioned purchases shall be performed at market prices to apply exemption.

The rates given above are standard rates. If a double tax treaty exists between Latvia and the relevant country, reduced rates or exemptions may be applied. A Latvian company paying the income to a non-resident company can apply these exemptions/lower tax rates only if the recipient of income has submitted the valid residence certificate stating that the recipient is resident in that country (certificate to be approved by tax authorities) before the actual payment is made.

A residence certificate should be approved by the local State Revenue Service office and is valid for five fiscal years.
G. EXCHANGE CONTROL

There is no exchange control in Latvia.

H. PERSONAL TAX

In 2016 Latvian residents are liable to personal income tax at a flat rate of 23% on their worldwide income. This includes all income (except income from capital and capital gains) after deductions such as social insurance contributions paid by employees, allowances, deductible expenses, unless specifically exempt. However, salary income earned by Latvian residents in another EU or EEA country or a country with which Latvia has a DTT is not taxed in Latvia provided income has been taxed in the other country. Benefits paid by EU/EEA countries to Latvian residents are tax exempt. Non-residents are liable to personal income tax at a flat rate of 23% on their Latvian source income. The tax year is the same as the calendar year. The same rate of 23% generally applies to salary income and to trading income. There are special rules for micro-companies paying micro-company tax.

All residents are entitled to a monthly non-taxable personal allowance which, in 2016, amounts to EUR 75, and an allowance for each dependent of EUR 175. As from 2016 differential personal allowance is introduced, which means that personal allowance for people on low wages will grow over the coming years, while those on high salaries will have a reduced level of personal allowance or none at all.

Tax in respect of salaries, bonuses and most other types of payments made by Latvian companies is withheld at source and remitted to the tax authorities. If the recipient of income is registered as a sole trader, he/she is responsible for calculating and paying income tax. Income from capital (such as interest and dividends) is taxed at a rate of 10% which is withheld at source. Dividend income is deemed to be earned when the dividend distribution decision is made (except in respect of dividends of public listed companies). The withholding tax must be paid to the tax authorities by the 5th day of the following month. Capital gains are taxed at a rate of 15%.

A capital gain is the difference between the selling price and acquisition cost of a capital asset, or the difference between any surplus assets received on a company's liquidation and the original investment, or the down payment on a sale that is not completed. Capital assets include shares, investments in partnerships, and other financial instruments, investment fund certificates, debt instruments, real estate, intellectual property.

Non-resident individuals shall pay tax on income (capital gain) from selling real estate and other capital assets, except publicly traded financial instruments. However, a disposal of shares in a company is deemed to be a disposal of real estate (and thus subject to 15% tax) when real estate comprises more than 50% of the company's total assets either during the year of disposal or in the previous year. The proportion of real estate is calculated at the beginning of the year.

Benefits from the private use of company vehicles are not subject to income tax provided the merchant pays light corporate vehicle tax on cars owned or held; the taxable amount depends on the engine capacity only. If light corporate vehicle tax is paid, car related expenses (fuel, maintenance, rent) can be treated as a deductible expense also for corporate income tax purposes.

SOCIAL INSURANCE CONTRIBUTIONS

Social insurance contributions are paid by both the employer and employee. The total rate for resident employees is 34.09% of gross employment income (including salary, bonuses, benefits in kind etc.), 10.50% of which is paid by the individual (withheld from gross salary) and 23.59% by the employer. Special rules apply to Latvian residents employed by foreign companies, foreign nationals employed by foreign companies (performing work in Latvia) and self-employed individuals.

In 2016 the income subject to social insurance contributions is still capped; the maximum amount per year is EUR 48,600. However, in 2016 the employer is required to continue calculating and paying amounts at the same rates as social insurance contributions, but these payments will be treated as
solidarity tax payments. Solidarity tax contributions will go to the core budget of the state.

I. TREATY AND NON-TREATY WITHHOLDING TAX RATES

Latvia has tax treaties with the following countries: Albania, Armenia, Austria, Azerbaijan, Belarus, Belgium, Bulgaria, Canada, China, Croatia, Czech Republic, Denmark, Estonia, Finland, France, Georgia, Germany, Greece, Hungary, Iceland, Italy, Ireland, Israel, Kazakhstan, Korea, Kyrgyzstan, Lithuania, Luxembourg, Macedonia, Malta, Mexico, Moldova, Montenegro, Morocco, Netherlands, Norway, Poland, Portugal, Romania, Russia, Serbia, Singapore, Slovak Republic, Slovenia, South Korea, Spain, Sweden, Switzerland, Tajikistan, Turkey, Turkmenistan, Ukraine, United Kingdom, United States and Uzbekistan.

Please note that the treaty has been concluded between Latvia and the former Serbia and Montenegro. From 2014, payments of dividends, interest and royalties by Latvian companies to non-resident companies are tax free. Management and consulting fees in general attract 10% withholding tax; zero rate is applied if DTT exemption applies (residence certificate submitted to the Latvian company paying income to non-resident).