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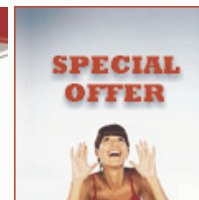


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NEWS

TALKING TAX: New regulation clarifies VAT application in Latvia

May 24, 2006
 By Janis Taukacs, Edgars Koskins

The government adopted new regulations on implementation of the Law on Value Added Tax. The regulations deal with interpreting and clarifying VAT and play a major role in leading businesses through the maze of VAT complexities. One of the material novelties implemented in the new regulation is derived from the case law of the European Court of Justice, which has ruled that a disposal of all or part of a business is a transaction not subject to VAT. Previously tax authorities held a position that such transactions were subject to VAT.

This new provision is extremely important for most purchases of a business (as opposed to share transactions), because as a minimum it would be an improvement for the cash flow of such transactions. To a great extent this provision is a result of thorough work by Sorainen tax lawyers, who represented these interests of several clients and pointed out to authorities the incompatibility of the Latvian law with the EU VAT Sixth Directive and the ECJ case law. It should be noted, however, that the introduction of the aforesaid improvement requires amending the Law on VAT.

Other novelties of the regulations deal with VAT in real estate transactions. First, there are clearer rules now for determining the taxable value of transactions with "unused immovable property." Second, it is clarified that the investment of an "unused immovable property" into a share capital is VAT-exempt, although the first sale of such property is subject to 18 percent VAT, which apparently leaves some room for VAT planning. Third, it is important to note for real estate businesses that now if a purchase price of the taxable ("unused") and exempt property has not been separated, then the entire purchase price will become subject to the 18 percent tax. Fourth, the procedure for paying VAT and for issuing of invoices in cases involving termination of hire purchase (leasing) agreements on "used immovable property" has been set.

The new regulations also explain the deduction of input VAT procedure for goods acquired or services received before a person has been registered in the VAT payer register, which is a new concept introduced by the Latvian law as of Jan. 1, 2006 thus implementing the corresponding ECJ case law. Also, the provisions on determining the market price (transfer-pricing) of a transaction and application of discounts and bonuses, etc., have been made more exact. Finally, although the new regulations have been published on May 8, 2005 it provides for a retroactive application as of April 2.

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