

TAX PROFILE, LITHUANIA

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KEY FACTS

Main tax rates

- Corporate tax rate: 15%
- VAT standard rate: 21%
- Personal income tax rate: 5% and 15%

Population/GDP

Population: 3.249 million

GDP: USD 36.8 billion (approx EUR 25.46 billion) (estimated for 2010)

Currency

Litas, abbreviated here to LTL (Lithuania is not part of the Euro zone but the litas is tightly pegged against the euro at a rate of LTL 3.4528 to EUR 1)

Membership of economic groups

European Union (EU), World Trade Organization (WTO)

Major industries

Services, retail and wholesale business, forestry

Website of tax/finance authority

<http://www.vmi.lt> – State Tax Inspectorate under the Ministry of Finance

<http://www.finmin.lt> – The Ministry of Finance

INTRODUCTION

The southernmost of the three Baltic States, Lithuania is situated along the south eastern shore of the Baltic Sea.

The principal source of taxation is personal income tax, corporate income tax, value added tax, and excise duty.

RECENT DEVELOPMENTS

The following are the most recent amendments to tax legislation in Lithuania.

Corporate income tax

Under the recent amendments annual bonuses paid to board members out of company profits are deductible for corporate income taxation purposes.

As of 2011, a corporate income tax return should be submitted within five months after the end of

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the taxable period. In this way the deadline for submitting annual corporate income tax returns for the tax year corresponding to the calendar year is 1 June (as opposed to 1 October applicable before 2011).

Personal income tax

The Law introduces a new term “professional occupation”, which is defined as a profession practiced by individuals having an appropriate qualification, in a responsible manner and independently from a professional point of view, by rendering intellectual services including legal, accounting, auditing, book-keeping, lobbying, financial consulting, tax advisory services, as well as architect, engineer, designer, journalist, broker and similar professions. The income of persons engaged in professional occupations and income from securities is subject to 15% personal income tax rate, ie taxation of such income has not changed as compared to 2010.

The personal income tax rate on income of self-employed individuals other than those engaged in professional occupations is reduced from 15% to 5%. This rate applies to income derived from production, trade and provision of the majority of services. The reduced rate applies in respect of income generated in 2010 and subsequent tax periods.

VAT

Application of a 9% VAT rate on heating energy, hot and cold water intended for heating of residential premises is extended to 31 December 2011.

Application of a 9% VAT rate on books and non-periodical information publications is extended indefinitely.

Application of a 5% VAT rate on fully or partially compensated medicines and means of medical aid is extended to 31 December 2011.

A 9% VAT rate on hotel and special accommodation services is introduced until 31 December 2011.

Real estate tax

As of 1 January 2011, real estate tax on real estate acquired by way of financial leasing will become payable by the person acquiring the property rather than by its actual owner (eg a financial institution leasing the property).

Real estate developed or acquired by way of public and private partnership is not subject to real estate tax for the period of the PPP agreement, provided that the property is used according to the designated purpose.

Furthermore, as of 1 January 2011 taxpayers may apply to the tax authorities for adjustment of the taxable value of immovable property.

Tax administration

With effect from 1 January 2012, advance tax rulings are introduced in Lithuania. Advance tax rulings are designed to enable taxpayers to apply to the tax authorities to confirm application of the provisions of tax legislation to a future transaction.

CORPORATE TAXES

General outline

Resident entities are taxable on their worldwide profits. An entity may deduct expenses related to business activity of the entity and earning income. However, the law establishes a list of expenses with limited deduction, as well as nondeductible expenses.

As a rule, nondeductible expenses are expenses that do not relate to earned income of the entity and are not related to its ordinary course of business activity, including certain expenses incurred due to related party transactions and transactions with offshore entities.

The list of expenses with limited deduction includes, for example: depreciation and amortisation of fixed assets; losses in a tax year, business trip related costs, marketing and promotional costs; natural loss and bad debts, taxes, and certain benefits granted to employees.

Standard rates of depreciation and amortisation are established by law. Rates of depreciation depend on groups of fixed tangible assets and vary from three up to 20 years (nonresidential purpose buildings – 15 years). In the case of intangible fixed assets, maximum rates of three or four years apply, while goodwill may be depreciated over 15 years. As a rule, fixed assets are depreciated or amortised according to the straight line method. However, for certain groups of fixed assets, including equipment and machinery, hardware and software, the double balance method may also be used. No depreciation is calculated for land.

Certain limitations apply to transfer of losses of entities under reorganisation.

Corporate tax rates

The general corporate income tax (CIT) rate is 15%. A reduced rate of 5% applies to small companies with income lower than LTL 500,000 (approx EUR 145,000) in one calendar year and less than ten employees.

Besides, a company with investments of EUR 1 million or more operating in a Free Economic Zone (Klaipeda and Kaunas) is exempt from income tax for six years and pays 50% of standard rate over the next ten years.

In principle, income of a foreign entity received through a permanent establishment (PE) situated in Lithuania is taxed following the same rules applied to taxation of income of Lithuanian entities. Income is taxed on an annual basis by applying a 15% tax rate.

Income of a Lithuanian entity's permanent establishment earned in a European Economic Area (EEA) Member State or in a country with which Lithuania has an effective double taxation treaty would not be included in the taxable base of the Lithuanian entity if such income has been subject to corporate income tax in that country.

Capital gains taxes

There is no specific concept of capital gains tax and, as a general rule, capital gains or losses are included in company taxable income. The main exception is capital gains on the sale of shares, which are exempt if they meet certain criteria, the main one being that the shares are held for three years. This does not apply where the seller is deemed to be consistently dealing in shares.

Under the general rule, capital gains of a nonresident company should be taxable only in its home country, except transfer of real estate and transfer of assets attributable to permanent establishment in Lithuania. Capital gains on sale of securities in a resident company are not taxable for nonresidents.

Position of losses

Losses may be carried forward for an unlimited period. Losses sustained from transfer of securities and derivative financial instruments may be carried forward only for five consecutive tax years. Those losses are accounted separately and may be covered only from profits from transfer of securities.

Losses incurred as a result of transfer of securities in entities registered or otherwise organised in an EEA Member State or other state with which a treaty on avoidance of double taxation is concluded

and which is a payer of corporate profit or similar tax, in which a transferring party has more than 25% of shares more than two years (or more than 25% of shares more than three years in the case of company reorganisation and transfer) may be set off against profit from transfer of securities during that tax period and losses not covered that cannot be carried forward to the next tax year.

Under Lithuanian law, an entity cannot carry losses backwards.

Intra group transfer of losses is available on the following conditions:

- The group parent company directly or indirectly holds at least 2/3 of the shares in both entities participating in loss transfer (or the loss may be transferred to the parent company).
- Both entities participating in the loss transfer must comply with this requirement for at least two years.

Alternatively, entities participating in a loss transfer transaction need to be within the group from its formation and have to remain in the group for at least two years.

Group treatment

Lithuanian tax laws do not allow taxation at company group level.

Position of resident companies

Resident companies are taxed on their worldwide income. Under the Law on Corporate Income Tax, gross revenue (total sales and nonoperating revenue) is the basis for computing taxable profit. Tax is applicable yearly. Income of a Lithuanian company's permanent establishment earned in a EEA Member State or in a country with which Lithuania has an effective double taxation treaty would not be included in the taxable base of the Lithuanian entity if that income has been subject to corporate income tax in that country.

Position of nonresident companies

Business profits of foreign entities are taxable only in their home countries unless foreign entities carry on business in Lithuania through a permanent establishment situated in Lithuania (in which case the taxation rules are similar to those attributable to resident entities) or receive income by means of cross border transfers that is subject to withholding taxes (including income received from lease or transfer of real estate, interest, dividends, royalties, or annual bonuses for supervisory board members).

Therefore, a nonresident company is subject to income tax in respect of income and capital gains attributable to permanent establishment.

WITHHOLDING TAXES

Dividends

Dividends paid by resident companies to residents and nonresidents are subject to withholding tax at a rate of 15%.

A participation exemption applies if a shareholder holds at least 10% of the voting shares in the distributing company for an uninterrupted period of twelve months, unless the shareholder is registered in a territory included in the black list (tax haven). The black list includes most of the typical offshore jurisdictions (approx 60 jurisdictions are listed).

According to official commentaries prepared by the Lithuanian tax authorities, dividends may enjoy the above participation exemption even if shares are held for a period shorter than twelve months but the shareholder intends to hold them for the same or a longer period.

This participation exemption satisfies the requirements of the EC Parent Subsidiary Directive.

The above rules apply irrespective of whether dividends are distributed from profits accumulated in periods prior to EU accession.

Interest

Interest paid to a company resident in an EEA Member State or in a country with which Lithuania has an effective double taxation treaty is subject to a withholding tax of 0%. Interest paid to other countries is subject to 10% withholding tax.

Royalties

Royalties are subject to a withholding tax of 10%.

Lithuania has been granted a six year transitional period to implement the Interest and Royalties Directive. Royalties paid to associated enterprises covered by the Interest and Royalties Directive (EU companies) will be exempt from withholding tax as of 1 July 2011.

Only the tax treaty with Latvia allows royalties paid to Latvian companies to be exempt from Lithuanian withholding tax.

Other

A withholding tax at the rate of 15% is levied on certain income of foreign entities sourced in Lithuania. This includes income from sale, other transfer into ownership or lease of immovable property in Lithuania, as well as income from performing activities and sports activities carried out in Lithuania, and annual bonuses to supervisory board members.

INDIRECT TAXES

VAT/GST: main and reduced rates, exemptions

General information

Lithuanian VAT legislation is based on the main principles set by the EU Sixth Directive.

Lithuanian VAT applies to supply of goods and services within Lithuania, import of goods into Lithuania, as well as to intra Community acquisitions that take place in Lithuania.

The standard VAT rate is 21%. A reduced rate of 9% applies to books and nonperiodical information publications, hotel and accommodation services and for residential heating, including water heating. A reduced rate of 5% applies to drugs covered from the Lithuanian budget under the Law on Health Insurance.

Certain supplies, such as transfer or lease of real estate, insurance and banking services, and share transfer are exempt from VAT.

According to the general rule, a VAT payer must calculate VAT and transfer it to the budget. VAT has to be paid within 25 days of the end of the taxable period. Entities where VAT payable exceeds LTL 100,000 (approx EUR 29,000) over three consecutive months have to make advance payments.

VAT registration

A resident taxable person must register as a VAT payer when its annual taxable turnover within the current twelve months exceeds LTL 100,000 (approx EUR 29,000).

Foreign taxable persons must register as VAT payers in Lithuania from the start of their business

activity if their place for VAT purposes is in Lithuania, except when they supply goods or services that 1) are exempt from VAT; 2) are not subject to VAT; 3) are taxed at a 0% VAT rate; or 4) obligate the purchaser/customer to calculate VAT.

Both resident and foreign taxable persons may apply for VAT registration, even if the obligation to register has not arisen. In order to comply with registration requirements, the taxable person must conduct or intend to conduct taxable activities. The tax authorities may request a taxable person to submit evidence of proof regarding actual or intended business activities.

Right to VAT deduction

As a general rule, only VAT payers have a right to VAT deduction and VAT refund.

A VAT payer may include input VAT in its deduction if the goods or services purchased are needed for supply of VAT taxable activity. In the case of mixed VAT activity, only a proportionate part of input VAT is deductible. Note that income from sale of real estate and securities should not be taken into consideration in calculating the proportion between VAT taxable and exempt activity, if sale of such assets is not a customary business activity of the VAT payer.

If output VAT calculated during a taxable period is less than the input VAT deductible during the same tax period, the VAT payer is entitled to a VAT refund.

Foreign taxable persons are also entitled to have paid Lithuanian VAT refunded. However, refund is subject to a number of restrictions.

Other indirect taxes

Lithuania applies excise duties (amongst other things) on petrol, alcohol, cigarettes and electricity.

PERSONAL TAXES

Domicile and residence requirements

An individual is deemed a resident of Lithuania if they are any of the following:

- Natural person with a permanent place of residence in Lithuania during a tax period.
- Natural person whose place of personal, social, or economic interests is in Lithuania rather than in a foreign country during a tax period.
- Natural person present in Lithuania for a period or periods for an aggregate of 183 days or more during a tax period.
- Any natural person present in Lithuania for a period or periods in the aggregate of 280 days or more during successive tax periods and who stayed in Lithuania for a period or periods in the aggregate of 90 days or more in any of such tax periods.

Main rates and bands

The general personal income tax rate is 15%.

A reduced rate of 5% applies on income of persons engaged in self-employed activities other than professional occupations. This rate applies to income derived from production, trade and provision of the majority of services.

The term “professional occupation” is defined as a profession practiced by individuals having an appropriate qualification, in a responsible manner and independently from a professional point of view, by rendering intellectual services including legal, accounting, auditing, book-keeping, lobbying, financial consulting, tax advisory services, as well as architect, engineer, designer, journalist, broker

and similar professions. The income of persons engaged in professional occupations and income from trade in securities is subject to a 15% personal income tax rate.

Fringe benefits

Under the general rule fringe benefits are taxed as income in kind of the recipient. As an exemption from the general rule, an exhaustive list of benefits is not regarded as income in kind. The list contains the following:

- nonmonetary gifts and prizes if not received from an employer and not exceeding LTL 320 (approx EUR 93);
- covering of medical treatment expenses by an employer when required by law;
- covering of expenses incurred while obtaining higher and university education;
- clothing, tools, and other equipment necessary for work provided by an employer;
- individual income tax, health insurance, and social security insurance contributions paid by an employer in the name and for the benefit of an employee.

All benefits granted to employees by Lithuanian companies that would fall outside the scope of this list would be regarded as fringe benefits and taxed as income in kind of employees.

Dividends

A 20% personal income tax rate has been imposed on income from distributed profits.

Social security insurance contributions

Employee rate – 3% withheld from gross salary; employer pays 27.98% on top of gross salary.

Different rates of state social security contributions exist for individual categories of persons (self employed, authors, sportsmen).

Health insurance contributions

Health insurance contributions contain a part payable by employers on behalf of employees (3%) and a part payable by employees themselves (6%). Health insurance contributions were previously included in social security insurance contributions.

Self employed persons engaged in individual activities pay health insurance contributions at a rate of 9% of taxable income earned during a calendar year from their individual activities subject to personal income tax (the tax base for the 9% contribution is capped at 48 annual monthly wages – LTL 56,160 (approx EUR 16,265) per year).

Tax administration (advance tax rulings)

With effect from 1 January 2012, advance tax rulings are introduced in Lithuania. Advance tax rulings are designed to enable taxpayers to apply to the tax authorities to confirm application of the provisions of tax legislation to a future transaction.

A taxpayer will be required to clearly specify the circumstances of the future transaction in the request and to indicate which provisions of tax legislation in their opinion should apply in the given situation. After the tax authorities receive the request, they confirm or deny assessment of the future transaction provided by the taxpayer. The decision is mandatory for the tax authorities throughout the period of the transaction (but not longer than five calendar years or by the date new legislation comes into force).

TRANSFER PRICING AND ANTI AVOIDANCE RULES

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Transfer pricing rules (documentation requirements, APAs, etc)

In summary, the relevant Lithuanian transfer pricing regulations can be listed as follows: requirement to 1) apply arm's length prices in related party transactions; 2) supply information to the Lithuanian tax authorities on related party transactions; and 3) maintain sufficient documentation of related party transactions.

Lithuanian transfer pricing regulations apply to Lithuanian entities, including branches and other permanent establishments of foreign entities. Lithuanian transfer pricing regulations have been prepared in line with OECD Transfer Pricing Guidelines for Multinational Enterprises and Tax Administrations, recommended for use to the extent that they do not contradict Lithuanian regulations.

It is noteworthy that Lithuanian law establishes a rather broad definition of associated entities and includes 1) related parties as defined by the Law on Corporate Income Tax; or 2) any other entities that may influence each other resulting in the conditions of their mutual transactions or economic operations other than those where maximum economic benefit is sought by each entity.

Under the Order, a fair market price is determined based on all five transfer pricing methods laid down in the OECD Guidelines. The comparable uncontrolled price method must be used first. If not enough data are available, the resale price or cost plus methods must be used. The profit split and transactional net margin methods have the lowest priority and can be used if data are insufficient to apply the first three methods.

Obligation to prepare written transfer pricing documentation

The obligation to prepare written transfer pricing documentation applies to companies which meet at least one of the following criteria:

- Lithuanian entities as well as foreign entities whose activities are carried out through a permanent establishment, if the income of the Lithuanian entity or income attributable to the foreign entity before the taxable year when the transaction was in fact carried out, exceeded LTL 10 million (approx EUR 2.9 million).
- Financial companies and credit institutions whose activities are carried out under the Law on Financial Institutions.
- Insurance companies whose activities are carried out under the Law on Insurance.

Content of documentation

Written transfer documentation should include:

- information about the transaction parties (economic and legal relationship, structure of MNE, cash flows, organisation of control within associated persons, information concerning other associated persons and other information);
- information about the controlled transaction (characterisation of the subject matter of the transaction, its functional analysis and conditions, economic circumstances, business strategy);
- information about the transaction method used and comparability (benchmarking) analysis (brief information how it was applied, what adjustments and calculations were made, what uncontrolled transactions were used, a functional analysis of uncontrolled transactions, economic circumstances, business strategy (if possible)); and
- other information identifying sufficient circumstances concerning transfer pricing.

It is noteworthy that Lithuanian law do not enable the mechanism of obtaining advance rulings in

related party transactions.

Anti avoidance provisions

There is a general anti avoidance provision in Lithuanian legislation known as the principle of substance over form. Where a taxpayer's transaction, economic operation, or any combination is concluded with a view to gaining a tax benefit (for example, directly or indirectly to defer the deadline for payment of tax, reduce the amount of tax payable or fully avoid payment of taxes, or shorten the time limit for refunding tax overpaid (tax difference)), the tax administrator may apply the substance over form principle for the purpose of calculating tax.

In this case, the tax administrator may not take into account the formal expression of the taxpayer's activity and may recreate distorted or hidden circumstances associated with taxation as provided for in tax laws and calculate tax under the relevant provisions of tax laws.

Thin capitalisation / other interest deductibility rules

Interest and currency exchange losses on debt in excess of a debt/equity ratio of 4:1 are nondeductible for corporate income tax purposes. This applies in respect of debt capital provided by a creditor, who:

- directly or indirectly holds more than 50% of shares or rights (options) to dividends, or
- together with related parties, holds more than 50% of shares or rights (options) to dividends, and the holding of that creditor is not less than 10%.

This rule does not apply if a taxpayer proves that the same loan could exist between unrelated parties. Financial institutions providing financial leasing services are not affected by this rule.

Notably, thin capitalisation also applies to interest variable depending on the profits or turnover of a company and costs of currency exchange results.

It should further be noted that under Lithuanian company law, the interest rate on shareholders' loans may not exceed the average bank interest rate valid in the location of the lender's business.

Controlled Foreign Company (CFC) rules

The CFC regulations apply to Lithuanian companies that directly or indirectly hold more than 50% of shares in a foreign company, provided that a foreign subsidiary is registered in:

- offshore territory or zone included in the black list;
- territory included in the white list, but enjoying a special privileged income tax regime in its home country; or
- in its home country is taxed at an income tax rate of less than three quarters of Lithuanian corporate income tax, that is 15%.

Lithuanian CFC rules apply both to active income and income gained from financial activity (for example, loan interest, financial lease, copyright remuneration).

However, active income of a foreign subsidiary is not attributed to income of a Lithuanian parent company if it satisfies establishment requirements.

Tax treaties

Lithuania has concluded 48 tax treaties. Table 1 shows the withholding tax rates established in treaties.

MISCELLANEOUS TAXES

Payroll taxes

There is no general payroll tax in Lithuania.

Taxes on capital

There is no capital contribution tax in Lithuania.

TAXES ON PROPERTY

Real estate tax

The annual real estate tax rate (applicable to real estate other than land) varies from 0.3% to 1% of the taxable value of real estate, depending on the decision of the particular municipality which has to determine the exact rate of tax within its area.

The annual land tax rate is 1.5% of land value.

OTHER TAXES

Stamp duty

Stamp duty on registration of a company or changes in share capital is not substantial (up to LTL 200 (approx EUR 58)).

It is noteworthy that registration of a company or changes in share capital must be notarised. Currently, notaries' fees may amount to LTL 1,000 (approx EUR 290).

Real estate transfer tax

There is no real estate transfer tax in Lithuania.

However, one should take into account stamp duty related to registration of ownership of real estate and costs of notarisation of real estate transfer.

State duties for registration of change of ownership rights to real estate are not substantial and vary depending on the market value of the real estate and whether the owner is a natural or legal person. Registration duties are calculated separately for each real estate object.

Notary fees amount to 0.45% of the value of the transaction, capped at LTL 20,000 (approx EUR 5,792).

Table 1 Tax treaty withholding rates

Country	Dividends		Interest (%)	Royalties ^a (%)
	Individuals, companies (%)	Qualifying companies ^b (%)		

^a The 5% rate mainly applies to use of industrial, commercial, or scientific equipment.

^b Reduced treaty rates will in most cases apply if a nonresident company owns at least 25% of the capital (or in some cases voting rights) in a Lithuanian company; no holding period is required. Please note that other conditions may apply to obtain a reduced rate.

Armenia	15	5	10	5/10
Austria	15	5	10	5/10
Azerbaijan	15	5	10	10
Belarus	10	10	10	10
Belgium	15	5	10	5/10
Bulgaria	10	0	10	10
Canada	15	5	10	10
China	10	5	10	10
Croatia	15	5	10	10
Czech Republic	15	5	10	10
Denmark	15	5	10	5/10
Estonia	15	5	10	10
Finland	15	5	10	5/10
France	15	5	10	5/10
Georgia	15	5	10	10
Germany	15	5	10	5/10
Greece	15	5	10	5/10
Hungary	15	5	10	5/10
Iceland	15	5	10	5/10
Ireland	15	5	10	5/10
Israel	15	5/10	10	5/10
Italy	15	5	10	5/10
Korea	10	5	10	5/10
Kyrgyzstan	15	5	10	10
Latvia	15	0	0	0
Luxembourg	15	5	10	5/10

Macedonia	10	0	10	10
Malta	15	5	10	10
Moldova	10	10	10	10
Netherlands	15	5	10	5/10
Norway	15	5	10	5/10
Poland	15	5	10	10
Portugal	10	10	10	10
Romania	10	10	10	10
Russia	10	5	10	5/10
Serbia	10	5	10	10
Singapore	10	5	10	7.5
Slovakia	10	10	10	10
Slovenia	15	5	10	10
Spain	15	5	10	5/10
Sweden	15	5	10	5/10
Switzerland	15	5	10	5/10
Turkey	10	10	10	5/10
Ukraine	15	5	10	10
UK	15	5	10	5/10
USA	15	5	10	5/10
Uzbekistan	10	10	10	10