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Tax&Legal Highlights

Latvia

The Constitutional Court has declared the Article 12.³ and the Article 12.⁵ of the Law On Value Added Tax insofar as they do not ensure the return of VAT overpayment to the taxpayer within a reasonable time, as not complying with the Article 105 of the Constitution of the Republic of Latvia.

According to the contested norms, the period during which VAT overpayments are returned to the taxpayer may range from approximately one month to one year and even longer.

This means that, according to the contested norms, VAT overpayment may also be returned to the taxpayer after a deadline that cannot be considered as reasonable. Such a transfer of VAT overpayment return period could be considered as complying with the principle of the neutrality of VAT, if the law would provide for the taxpayer compensation of the taxpayer's financial loss, resulting from such delay, with late payment interest.

However, compensation for the financial burden resulting from the transfer of VAT overpayment return period late payment interest is not provided in the contested norms of the Law On Value Added Tax. Consequently, the contested norms creates for the taxpayer a financial burden, which is not compensated. This means that the impugned norms do not comply with the principle of VAT neutrality.

Consequently, the restriction of fundamental rights established in the contested norms is not proportionate and the contested norms are to be declared as not complying with the Article 105 of the Constitution of the Republic of Latvia.

The Applicant asked for the contested norms to be recognized, insofar as they limit the right to return VAT overpayment within a reasonable time, as not complying with the first, second and third sentences of the Article 105 of the Constitution of the Republic of Latvia.

According to the Applicant's opinion, the damage, which takes the form of a financial burden and which arises from the transfer of the term of the return of the overpaid tax defined in the contested norms, is higher than the benefits that the society derives from the country resource savings resulting from this transfer. Consequently, the restriction of the taxpayer's fundamental rights, established in the contested norms, is not proportionate.

The Constitutional Court came to conclusion that the contested norms create the restriction of the taxpayer fundamental rights set forth in the first three sentences of the Article 105 of the Constitution of the Republic of Latvia.

The Constitutional Court also establishes that the restriction of fundamental rights established in the contested norms has a legitimate aim - the protection of the welfare of society and that the means chosen by the legislator are suitable for achieving the legitimate aim.

The Constitutional Court acknowledges that there are no more lenient means that would ensure the same amount of state resources savings as it is provided, if the state does not need to make a significant part of administrative activity at all.

According to the contested norms, the period during which VAT overpayments are returned to the taxpayer may range from approximately one month to one year and even longer. This means that, according to the contested norms, VAT overpayment may also be returned to the taxpayer after a

deadline that cannot be considered as reasonable. Such transfer of VAT overpayment return period could be considered as complying with the principle of the neutrality of VAT, if the law would provide for the taxpayer compensation of the taxpayer's financial loss, resulting from such delay, with late payment interest. However, compensation for the financial burden resulting from the transfer of overpayment return period late payment interest is not provided in the contested norms of Law On Value Added Tax. Consequently, the contested norms create for the taxpayer a financial burden, which is not compensated. This means that the contested norms do not comply with the principle of VAT neutrality.

Consequently, the restriction of fundamental rights established in the contested norms is not proportionate and the contested norms are to be declared as not complying with the Article 105 of the Constitution of the Republic of Latvia.

The contested norms have already expired since January 1, 2013, when the Value Added Tax Law entered into force. However, contested norms can still be applied to the already initiated, but not closed administrative proceedings, based on the legitimacy of the State Revenue Service decisions adopted on the basis thereof.

The Cabinet of Ministers approved amendments to the Law on Taxes and Duties with a view to improving the legal framework for transfer pricing documentation

The transfer pricing documentation requirements contained in the draft law will be more specific compared to the current general requirements. As a result, taxpayers will have a clearer regulatory framework and, when preparing transfer-pricing documentation, the taxpayer will be able to rely on law regulation more than on OECD transfer pricing guidelines, as it mostly takes place at the moment.

The transfer pricing documentation is a set of documents prepared by the taxpayer to substantiate that the transaction price (value) of an associated foreign entity corresponds to the market price. The statutory provision will decrease the possibility of shifting corporate profits to a country with more favourable tax treatment by manipulating the value of transactions.

The requirements of the transfer pricing documentation revised by the amendments to the law are suited to the current situation in which more and more companies in the same group of companies, each of them residing in a different country, are involved in the provision of the same service or supply of the same goods. In such cases, transfer pricing documentation needs to provide information on the entire business group's overall economic activity. Transfer pricing documentation will consist of two parts: global documentation (information for the entire group as a whole) and local documentation (information about a particular transaction, including price calculation).

At the same time, the thresholds at which taxpayers are required to make transfer-pricing documentation are increased. This will reduce the administrative burden for smaller transactions. In turn, transfer pricing documentation for transactions between Latvian associated companies will have to be prepared only when requested by the State Revenue Service. Therefore, transfer-pricing requirements will apply to a smaller range of taxpayers.

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The amendments to the law also includes other changes, including that the competent authority of the mutual reconciliation procedure is the State Revenue Service and amendments also intends to improve the separate components of the tax audit legal framework.

The Committee of the Cabinet of Ministers has conceptually supported the draft of the Residential Tenancy law

The Committee of the Cabinet of Ministers on April 23, 2018 conceptually has approved the draft of the Residential Tenancy Law, which will be a new regulation in the residential real estate market and will promote the creation of qualitative and affordable rental apartments, will offer a new solution to the ongoing long litigation processes, as well as promote investments in the rental real estate sector.

In order to reduce the shadow economy, the new draft law prescribes registration of all rent agreements in the Land Register, thus providing publicly available and reliable information on concluded rent agreements that will protect both tenants and new real estate owners. It is important to emphasize that registration of a rent agreement in the Land Register will be free of charge, thus not creating additional costs for the lessor and the tenant. Simultaneously, registration of a tenancy agreement in the Land Register will allow the elimination of fictitious rental agreements as well as protecting honest tenants in the event of a change of lessor.

The new draft law will also significantly accelerate the settlement of disputes between the lessor and the tenant and will reduce the associated costs. The current law provides the settlement of all disputes in court. With the new law, by making appropriate amendments to the Civil Procedure Law, there is offered an uncontested execution of obligations in certain cases (in cases where there is no dispute) - the tenant will be obliged to leave the rented residential space if the term of the lease has expired and new agreement will not be reached, if there is a rental payment debt, as well as in the event of the sale of real estate, if the rental agreement is not registered in the Land Register. At the same time, such a solution will significantly reduce the risks for potential investors to invest in the building of new rental real estate.

Significant changes are prescribed in terms of the term of the lease agreement - the lease agreement can no longer be concluded for an indefinite period. The rent agreement will only be concluded for a certain period of time, and upon expiry of the term, the tenant will be obliged to leave the living space, unless a new rental agreement is concluded with the lessor. Same as before, a tenant will be able to cancel the contract without any special reason by notifying the lessor in advance; while the lessor will still be able to withdraw the contract only in cases and within the time limits specified by the law.

The rights of the tenants' family members will also be affected - members of the family will no longer enjoy an independent right to use the living space, thus the members of the family will no longer be jointly and severally liable for the obligations arising from the rent agreement. Only in the event of the death of the tenant, family members are entitled to request a new rent agreement without changing the terms of the previous rent agreement.

With a view to protecting the tenants' interests more effectively, the draft law stipulates that the lessor will be able to increase the rent payment only

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if the rent agreement will specify the principles and procedures for raising a rent payment.

In accordance with the transitional provisions rental agreements that were concluded prior to the entry into force of the new law shall be registered in the Land Register within 5 years from the entry into force of the law.

Within two years from the entry into force of the law, the lessor and tenant who currently uses the living space on the basis of the lease agreement concluded with the previous lessor, must conclude a new rental agreement

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