



Expert advice

Tax disputes in Estonia and Latvia
Alice Salumets, attorney-at-law, Estonia
Ellīna Putniņa, certified tax consultant, Latvia

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General stages of tax proceedings

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Main topics of tax dispute

The general stages of tax proceedings

Estonia

- 1. Tax examination**
- 2. Notice of assessment**
- 3. Challenge**
- 4. Right to appeal**
- 5. Liability decision proceeding**

Latvia

- 1. Tax examination**
- 2. Notice of assessment**
- 3. Challenge**
- 4. Right to appeal**

Agenda

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General stages of tax proceedings

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Main topics of tax dispute

The eight main tax dispute topics in Estonia:

- 1. The buyer-seller disputes**
- 2. Liability decision**
- 3. Shareholders disbursements**
- 4. Fringe benefits**
- 5. Capital gains**
- 6. Property and VAT**
- 7. The place of supply of goods and services**
- 8. Tax evasion**

The buyer-seller disputes (VAT disputes) (I)

Main questions in “buyer-seller” disputes:

1. Are the goods / services “real”? Did the transaction really took place?
2. Is the seller on the invoice the actual seller (the “real” seller)?

The first two questions are the main questions of the “buyer-seller” disputes. If one of these questions can be answered as questionable or with yes, then tax authorities will continue their investigation.

The buyer-seller disputes (VAT disputes) (II)

3. Who are the “real” parties of the transaction?
4. Did the buyer "knew" that the seller on invoice was not the “real” seller?
 - Knew - direct evidence
 - Knew - through participation in tax evasion
 - Knew - circumstantial evidence collection
 - Collection of evidence

The buyer-seller disputes (VAT disputes) (III)

5. Did the buyer “ought to know” that the seller on the invoice was not the “real” seller?
 - Due diligence
 - due diligence (written rules of business/required by law)
 - due diligence (unwritten rules of business)
 - Ought to know

The buyer-seller disputes (VAT disputes) (IV)

Estonia:

6. Limitation period for making assessment of tax:
- Three years (“ought to know”)
 - Five years (“knew”)

Latvia:

6. Period to audit or amend tax report – three years in all cases.

The limitation period for making an assessment of tax is three years. In the event of intentional failure to pay or withhold a tax, the limitation period for making an assessment of tax is five years. A limitation period begins to run on the due date for the submission of the tax return which was not submitted or which contained information which caused the amount of tax to be calculated incorrectly.

Liability decision in Estonia (I)

In order to collect tax arrears from a third party who is liable for the performance of obligations of a taxpayer or withholding agent pursuant to law, a tax authority shall make a liability decision.

The basis of the tax arrears:

- Notice of assessment;
- Declared tax arrears.

Who are the third parties:

- member of the management board;
- shadow director.

Liability decision in Estonia (II)

A liability decision is not made if:

- no tax arrears have been incurred;
- the limitation period for the collection of the tax arrears has expired;
- the tax arrears have been forgiven.

Liability decision in Estonia (III)

The basis of the liability:

The types of culpability are gross negligence and intent (carelessness is not the basis of the liability).

- Gross negligence is failure to exercise necessary care to a material extent.
- Intent is the will to bring about an unlawful consequence upon the creation, performance or termination of an obligation.

Tax authority has the obligation to evaluate all third parties culpability separately.

Liability decision in Estonia (IV)

Limitation period for making assessment of tax:

- Three years (gross negligence)
- Five years (intent)

Liability of members of board for tax debts - Latvia (I)

General information:

- Introduced in law in 2014, in force from January 1st, 2015.
- Can be applied on tax debts occurred after January 1st, 2015.
- Aim of the amendments – prevention. The tax administration has planed that procedure will be applied few times.
- Procedure can be commenced against member of the board who held the position when tax debt aroused.

Liability of members of board for tax debts - Latvia(II)

Criteria to start the procedure – all of them must be fulfilled:

- Tax debt exceeds amount of 50 minimal wages (EUR 18 500 in 2016).
- Legal person has been informed about decision to collect debt.
- After commencement of the tax debt legal person has disposed assets to interested party in a meaning of Insolvency law.
 - If assets are disposed for market price – this criterion is not fulfilled.*
- Deed has been prepared confirming that it is not possible to recover tax debt from legal person.
- Legal person has not submitted request to start insolvency procedure according to Insolvency law

Liability of members of board for tax debts - Latvia (III)

Decision about reimbursement of delayed tax debts:

- If all mentioned criterions have been met the tax administration issues warning about the decision.
- If within 15 days insolvency procedure of the company is started or tax debt paid – the procedure to collect tax debts is terminated.
- Member of the board can ask the tax administration to terminate the procedure, if:
 - Insolvency procedure was not initiated because of objective reasons;
 - Disposal of assets to interested person is economically justified;
 - Member of the board is not liable for tax debts and disposal of assets.If application is justified – the procedure is terminated.
- Decision about reimbursement of delayed tax debts can be appealed in the Administrative court. It can be enforced only when all appeal stages have been used.

Liability of members of board for tax debts – Latvia (IV)

How does it work in practice:

- No case so far in our practice.
- According to the law home page of the tax administration should contain information about started procedures – no such information has been published.
- Requested has been submitted in the The Constitutional Court to solve the dispute if the regulations comply with the Constitution of Latvia.
- It is advisable to members of the boards to be informed about the procedure and, if needed, perform all measures to avoid it.

Disbursements to the shareholders (Income tax disputes)

Main topics:

1. "The transaction has not taken place" - the payment is made without legal basis
2. "ought to know", or breach of duty of care (same questions as before with VAT disputes ("buyer-seller"))
3. "Knew" the situation (same questions as before with VAT disputes ("buyer-seller"))
4. Payment and taxation of the difference in price
5. The distinction between goods and services evaluation
6. The legal basis of taxation (different legal basis of income tax)

Fringe benefits (income tax and social tax) (I)

Fringe benefits are any goods, services, remuneration in kind or monetarily appraisable benefits which are given to an “employee” in connection with an employment or service relationship, membership in the management or controlling body of a legal person, or a long-term contractual relationship, regardless of the time at which the fringe benefit is granted.

For example fringe benefits include:

1. full or partial covering of housing expenses;
2. the use of a vehicle or other property of the employer free of charge or at a preferential price for activities not related to employment or service duties or to the employer’s business;
3. payment of insurance premiums, unless such obligation is prescribed by law.

Fringe benefits (income tax and social tax) (II)

Main questions:

1. Who is the employer on the legal basis?
2. Who is the employee on the legal basis?
3. What were the goods/services that the employee/members of management board received?
4. Are these goods/services connected to the economic activities of the company?
5. How the employee/member of management board enriched at the expense of the company?

Capital gains of the taxpayer (income tax) (I)

Main topics:

1. Income tax on expenses not related to business and activities specified in articles of association
2. Income tax on other payments not related to business
3. Fringe benefits vs payments not related to business
4. Taxation of inheritance (acquisition cost)
5. Acquisition cost
6. Income from “crowdfunding”
7. Gains from the transfer of the taxpayers place of residence

Capital gains of the taxpayer (income tax) (II)

Some guiding questions:

1. What are the expenses not related to business?
2. Who has to obligation to declare his/her capital gains in Estonia?
3. What capital gains are taxed with income tax/what are excluded?

Capital gains of the taxpayer (income tax) (III)

Income tax is charged on gains from the sale or exchange of any transferable and monetarily appraisable objects including:

1. real or movable property,
2. securities,
3. registered shares,
4. contributions made to a general or limited partnership or an association,
5. units of investment funds, rights of claim, rights of pre-emption,
6. rights of superficies,
7. usufructs,
8. personal rights of use,
9. rights of commercial lessees,
10. redemption obligations,
11. Mortgages;
12. etc.

Capital gains of the taxpayer (income tax) (IV)

- The gains or loss derived from the sale of property is the difference between the acquisition cost and the selling price of the sold property.
- The gains or loss derived from the exchange of property is the difference between the acquisition cost of the property subject to exchange and the market price of the property received as a result of the exchange.
- A taxpayer has the right to deduct certified expenses directly related to the sale or exchange of property from the taxpayer's gain or to add such expenses to the taxpayer's loss.

Acquisition cost means all certified expenses which a taxpayer makes in order to obtain, improve or supplement property, including any commissions and fees paid.

Property and VAT

Main topics:

1. Commercial real estate
2. Dwellings
3. The specific purpose of the registered immovable property

According to the VAT Act a taxable person shall add value added tax to the taxable value of the following goods and services if the person has, during the same taxable period or earlier, notified the Estonian Tax and Customs Board thereof in writing before the supply is effected:

- the leasing or letting of immovables or parts thereof, except dwellings, and establishment of a usufruct on immovables or parts thereof;
- immovables and parts thereof, except dwellings;

The place of supply of goods and services

Main questions:

1. When is/is not the place of supply of goods Estonia?
2. When is/is not the place of supply of services Estonia?
3. *Triangular transactions

Tax evasion

Main questions:

1. Taxation Act § 84 defection – tax evasion (What does tax evasion in Estonia mean (tax evasion vs tax avoidance))?
2. What is “actual economic content of the transaction”?

If it is evident from the content of a transaction or act that the transaction or act is performed for the purposes of tax evasion, conditions that correspond to the actual economic content of the transaction or act apply upon taxation.

Your contact



Alice Salumets

Partner

Rödl & Partner Advokaadibüroo

Tartu mnt 13

10145 Tallinn

Phone +372 606 8650

Mobile phone + 372 5077770

alice.salumets@roedl.pro



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