

Lithuania Highlights 2010

Currency: Lithuanian Litas (LTL)

Foreign Exchange Control: No

Accounting principles/financial statements: IAS and IFRS or Business Accounting Standards (BAS). BAS are prepared in conformity with IAS, IFRS and the European accounting directives. Financial statements must be prepared annually.

Principal business entities: These are the public/private limited liability company, general/limited partnership, subsidiary of a foreign enterprise, and (not considered a legal entity) branch or representative office.

Corporate taxation:

Residence – A corporation is resident if it is incorporated in Lithuania.

Basis – Lithuanian entities are subject to tax on their worldwide income minus the income of their permanent establishments provided that the permanent establishments are based in EEA countries or in countries with which Lithuania has concluded double taxation treaties.

Non-resident entities are subject to tax only on income sourced in Lithuania, as well as on income received by a permanent establishment in Lithuania.

Taxable income – Corporate income tax is imposed on a company's profits, which consist of business/trading

income, passive income, capital gains and positive income of a Lithuanian entity's controlled foreign entity or part of such income. Normal business expenses may be deducted in computing taxable income.

Taxation of dividends – Dividends are taxable at a rate of 15% unless the participation exemption (i.e. dividends are corporate income tax exempt if a parent company holds at least 10% of shares for at least 12 months) applies.

Dividends received from foreign entities which are registered in the states of EEA are exempt from tax. In case a Lithuanian entity distributes its profits to individual shareholders, and the profits (part thereof) were exempted from corporate income tax due to application of corporate income tax incentives, such distribution results into the taxation of the proportionate part of the distributed profits at the rate of 15%. The latter only applies to profits accumulated in 2009 and following years.

Capital gains – Capital gains of resident and non-resident companies are taxed as general taxable income at a rate of 15%.

Exemption on capital gains – An exemption may apply to capital gains derived by a Lithuanian resident holding company or a permanent establishment of a foreign company (certain additional

requirements) on the disposition of shares in a company (which is subject to corporate income tax) located in Lithuania, another EU or EEA member state or a country that has concluded a tax treaty with Lithuania. To qualify for the exemption, the Lithuanian company or permanent establishment must hold more than 25% of the voting rights for an uninterrupted period of at least 2 years. In case of reorganization (provided that it is performed in compliance with the respective rules of Law on Corporate Income Tax), the exemption applies if a company or a permanent establishment has held more than 25% of the voting rights for an uninterrupted period of at least 3 years.

Losses – Operational losses can be carried forward for unlimited period if the entity continues carrying on the activity which resulted losses. Losses from the sale of securities may be carried forward for 5 years and may only be offset against income from the sale of securities.

As of 1 January 2010 losses can be transferred within group of companies provided certain criteria are met.

Rate – The generally applicable rate is 15%, but micro companies (up to 10 employees and income per year – up to LTL 500,000) under certain conditions may be entitled to a reduced rate of 5%.

Surtax – No

Alternative minimum tax – No

Foreign tax credit – Foreign tax paid may be credited against Lithuanian tax on the same profits, but the credit is limited to the amount of Lithuanian tax payable on the foreign income. An exemption applies under some of Lithuania's tax treaties.

Holding company regime – Lithuania does not have a holding company regime, but an exemption on capital gains in case of disposal of shares may be available (please see "Exemption on capital gains").

Incentives – Incentives are provided for micro companies and for free economic zone companies.

As of 1 January 2008 CIT incentive is applicable to the scientific research and experimental development costs. When calculating CIT, the scientific research and experimental development costs are deducted three times from income.

An incentive on investments into substantial technological improvements entitles the companies to reduce the taxable profit down to 50%. This CIT incentive will be applicable to the expenses incurred during years from 2009 to 2013.

Withholding tax:

Dividends – The withholding tax on dividends is 15%. The rate may be reduced under an applicable tax treaty or exempt under the EC parent-subsidiary directive.

Interest – The withholding tax is 10% for interest paid to non-resident companies unless reduced under a tax treaty. As of 1 January 2010 withholding tax on interest was abolished for EEA companies and resident companies of countries with which Lithuania has concluded double taxation treaties.

Royalties (and compensations for violation of copyright or related rights) – The withholding tax is 10% for royalties paid to non-resident companies unless reduced under a tax treaty. The 10% withholding tax on EU affiliated companies will be abolished from 1 July 2011 in accordance with the transition period provided in the EC interest and royalties directive.

Branch remittance tax – No

Other taxes on corporations:

Capital duty – No

Payroll tax – No

Real property tax – Depending on the municipality the rate varies from 0.3% to 1% of the value of real estate owned by legal persons or owned by individuals and transferred for use to legal persons for an indefinite period or for a period exceeding 1 month. The type of property involved will determine the applicable valuation method and thus the taxable amount.

Social security – In addition to withholding 3% pension social insurance contributions and 6% health insurance contributions on behalf of an employee, an employer must contribute to social insurance (including pension social insurance, sickness and motherhood social insurance, unemployment insurance, health insurance, occupational accidents and diseases contributions) at a rate of 30.98% - 31.7% of the employee's gross salary depending on the risk group.

For social security contributions on royalties paid to individuals please refer to section "Other taxes on individuals".

Stamp duty – No. A notary fee, however, may apply to some transactions.

Transfer tax – No

Other – An employer must contribute 0.1% of an employee's gross wages to the Guarantee Fund.

Anti-avoidance rules:

Transfer pricing – Lithuania's transfer pricing rules are based on the OECD transfer pricing guidelines. Companies must document transfer prices if the annual turnover exceeds LTL 10 million (the threshold does not apply to financial and credit institutions and insurance companies).

Thin capitalisation – Thin capitalisation restrictions apply to interest paid to controlling entities. The creditor qualifies as a controlling entity if it owns more than 50% of the shares in the company paying the interest (or more than 50% of the shares are owned together with associated persons and the "own" holding is 10% or more). A group company also qualifies as a controlling entity. A debt-to-equity ratio of 4:1 applies, and any interest attributable to the debt in excess of this ratio is non-deductible. Thin capitalisation restrictions do not apply if the paying entity can demonstrate that the same loan would have been granted under the same circumstances by an unrelated party. No thin capitalisation restrictions apply to third party loans (e.g. loans from banks or other financial institutions).

Controlled foreign companies – A foreign company is treated as a CFC if it is controlled by the controlling person on the last day of the tax period and the controlling person holds directly or indirectly more than 50% of the shares (or the controlling person, together with related persons, holds more than 50% of the shares and the portion controlled by the controlling person accounts for at least 10% of the shares) in the controlled entity or other rights to a portion of distributable profits or pre-emptive rights to the acquisition thereof.

Other – The substance-over-form principle applies under the statutory GAAR provisions.

Disclosure requirements – No

Administration and compliance:

Tax year – Tax year is a financial year which coincides with calendar year. However, at the request of the taxpayer and taking into account the characteristics of its activity, the tax authorities may set a tax period other than a calendar year subject to condition that the tax period is 12 months.

Consolidated returns – Consolidated returns are not permitted; each company must file a separate return.

Filing requirements – Companies make advance payments of corporate income tax on a quarterly basis, with the final balance due on the same date as the annual tax return, i.e. 1 October of the following tax year.

Penalties – Penalties equal 10%-50%, depending on the type of violation, the taxpayer's cooperation with the tax authorities and other circumstances the authorities deem relevant. For late tax payment, daily late charges equal to 0.05% apply starting from 1 April 2009.

Rulings – Rulings are available, however, they are not binding on the tax authorities or on the tax payer.

Personal taxation:

Basis – Lithuanian residents are subject to tax on their worldwide income; non-residents are subject to tax only on income sourced in Lithuania and income derived from activities through a fixed base in Lithuania, including foreign-source income attributed to that fixed base.

Residence – An individual is treated as a resident if at least one of the following conditions is met: (1) the individual's permanent place of residence is in Lithuania during the tax period; (2) the

individual's personal, social or economic interests are in Lithuania rather than abroad during the tax period; (3) the individual is present in Lithuania for at least 183 days during the tax period; (4) the individual is present in Lithuania for at least 280 days during the 2 consecutive tax periods and has stayed in Lithuania for at least 90 days in any of such tax periods; or (5) the individual is a citizen of Lithuania who does not meet the criteria set out in (3) and (4) above and who receives employment-related remuneration or whose costs of living in another country are covered by the state budget or municipal budgets of Lithuania (e.g. diplomats, consuls, etc.).

Filing status – Joint filing is not allowed.

Taxable income – Taxable income includes income from individual commercial activities, royalties, the lease of assets and other qualifying income, employment income and all other personal income.

Capital gains – Individuals are taxed at 15% personal income tax on gains from the disposal of property, including shares. Gains on the disposal of shares that have been held continuously for at least 366 days are exempt, subject to certain requirements (including the requirement that the ownership of the seller together with associated persons during the previous 3 years does not exceed 10% of the share capital).

Capital gains from the sale of immovable property located in the EEA are exempt if owned for at least 3 years before the sale (unless the sale of immovable property constitutes the business activities of the individual). In case of transfer of residential premises, the income will not be taxable provided that the domicile was declared in those residential premises for at least 2 years or when less than 2 years – when the income from the sale is used (within one year) to obtain other residential

premises where the domicile will be declared.

Deductions and allowances – The annual tax exempt amount (TEA) of LTL 5,640 is applicable if annual income does not exceed LTL 9,600. Annual TEA is reduced accordingly if annual income is from LTL 9,600 to LTL 37,800. No TEA is applicable if annual income exceeds LTL 37,800. The annual TEA is calculated taking into account all income received (not only employment income). Additional TEA is deducted from income received by individuals raising children: additional TEA of LTL 1200 is deducted for 1 child, additional TEA of LTL 2400 is deducted for the second and each subsequent child. Additional TEA is divided for both parents equally not depending on the income received by any of them. Furthermore, deductions for life insurance, pension funds and vocational training or study are possible (however, subject to certain limitations).

Residents carrying out individual business activities can deduct 30% of their annual income without holding any documental proof of such expenses. If an individual wishes to deduct more than 30% of the income he/she will be required to hold documented proof of such costs. Deductible costs for individual activities are similar (with some exceptions) to those for corporate income tax purposes.

Rates – All income of individuals (except dividends and other profit distributions) is subject to personal income tax at the standard rate of 15%. Dividends and other profit distributions will be taxed at the personal income tax rate of 20%. Income received by an owner of an unlimited civil liability entity from the entity's taxable profits is taxed at 15% personal income tax rate.

Other taxes on individuals:

Capital duty – No

Stamp duty – There is no stamp duty but a notary fee may apply to some transactions.

Capital acquisitions tax – 15% personal income tax is levied on gifts having a value greater than LTL 8,000. Only the portion of the gift exceeding LTL 8,000 is subject to tax.

Gifts received from a spouse, child, brother, sister, parent or grandparent are tax exempt.

Real property tax – The rate ranges from 0.3%-1% of the value of real estate owned by individuals, depending on the municipality.

Individuals are obliged to pay the Real property tax for buildings if they are used in individual or economic activity.

Buildings intended for certain purposes (manufacturing, industry, nourishment, services, trading, hotels, etc.) are subject to Real property tax, regardless if they are used in individual or economic activity or not. The latter is not applied if the buildings are rented or transferred on the basis of loan- for-use contract to legal entities.

The type of property involved will determine the applicable valuation method and thus the taxable amount.

Inheritance tax – The inheritance tax rate is 5% of inheritable assets valued at LTL 500,000 or less and 10% on inheritable assets valued at more than LTL 500,000. However, the taxable base is only 70% of the inherited assets. Furthermore, the taxable value not exceeding LTL 10,000 is exempt. The exemptions also apply to assets inherited by family members.

Net wealth/net worth tax – No

Social security and health insurance – Employers withhold 3% pension social insurance contributions and 6% health insurance contributions on behalf of employees.

Royalties received from employer are subject to 6% health insurance contribution and 2% social security contribution in 2010 (starting from 2011 social security contribution is 3%). In addition, the entity that pays the income, i.e. the insurer, must pay 3% health insurance contribution and 14% social security contribution in 2010 (starting from 2011 social security contribution is 28%).

Royalties received from entity other than employer are also subject to 6% health insurance contribution and 3% social security contribution. In addition, the entity paying the income must pay 3% health insurance contribution and 26.7% social security contribution. Basis for health and social security contributions is 50% of the income with a cap of 48 times the annual insured income (currently LTL 1,170 x 48).

Income from individual activities is subject to 9% health insurance contributions (except for those derived when holding a business certificate). This income is also subject to social security contributions at the rate 28.5%. Caps for both health insurance and social security contributions are set. They are set in a way that annual contributions are calculated on amount of income not exceeding 48 times the annual insured income (currently LTL 1,170 x 48). As of 1 January 2010 base of health insurance and social security contributions is 50% of taxable income before the deduction of health insurance and social security contributions.

Income of owners of unlimited civil liability entities and members of partnerships currently is subject to 6% health insurance contributions due by the owner/member receiving the income and 3% by the unlimited civil liability entity/partnership. Income of owners of unlimited civil liability entities and members of partnerships is also subject

to 28.5% social security contributions. The base of these contributions is the remuneration received by the owners of unlimited civil liability entities and members of partnerships, which has to be agreed upon with the local office of the State Social Security Fund and State Tax Inspectorate. The monthly amount remuneration cannot be lower than the minimum statutory monthly salary (currently LTL 800). Caps for both health insurance and social security contributions are set. The maximum amount on which the contributions are calculated is 48 times the annual insured income (currently LTL 1,170 x 48).

Health insurance contribution on *income derived from carrying individual activities with a business certificate* is 9% of monthly minimum salary (currently LTL 800). Social security contributions on such income - 50% of the base pension benefit (currently the contribution amounts to LTL 180 per month).

Income of sportsmen, income from entertainment activities, income from farming activities and certain other types of income are subject to special provisions in respect social security and health insurance contributions.

Administration and compliance:

Tax year – Calendar year

Filing and payment – Employment income is taxed by withholding at source. Individual tax returns are due by 1 May following the end of the taxable year.

Penalties – See under "Corporate taxation".

Value Added Tax:

Taxable transactions – VAT applies on the sale of goods and provision of services.

Rates – The standard rate as of 1 September 2009 is 21%, with reduced rates of 9% (for books and not periodical

press until 31 December 2010 and for heating energy, supplied to residential premises and for the purpose of water heating as well as water for heating until 31 August 2010), 5% (certain pharmaceutical products (until 31 December 2010)), and 0% (e.g. exports, insurance and financial services related to export, transport services directly related to the export of goods and goods supplied to another EU member state).

Registration – Registration is compulsory for Lithuanian businesses whose annual turnover exceeds LTL 100,000, but voluntary registration also is possible. The turnover threshold does not apply to foreign companies; they must register irrespective of turnover. Foreign taxable persons must register either through a local affiliate or through

a fiscal agent. Only companies established in an EU member state may register directly.

Filing and payment – VAT is paid on a monthly basis, no later than 25 days after the end of the taxable period. In some instances, a calendar half year or other taxable period basis can be applied. If average monthly income exceeds LTL 100,000 (LTL 200,000 for companies engaged in construction work) for three months in a row a company is required to pay advance VAT payments thrice a month. The annual tax return is due on 1 October of the following tax year.

Source of tax law: Tax Administration Law, Corporate Income Tax Law, Personal Income Tax Law, Law on Health Insurance, Law on Social

Security Contributions, Value Added Tax Law, etc.

Tax authorities: State Tax Inspectorate under the Ministry of Finance of the Republic of Lithuania, Customs Department of the Republic of Lithuania, the State Social Insurance Fund Board under the Ministry of Social Security and Labour

International organisations: EEA, EU, WTO

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