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A private limited company may be founded by one or more persons that may be individual or legal persons (local or/and foreign).

The founders must execute an agreement on establishment or an establishment act (in the case of the sole founder). The founders must also approve the articles of association of the company as well as fill in standard application forms to be provided to the Register of Legal Persons where all companies are registered. All the above documents must be duly approved by a Lithuanian notary public and afterwards provided to the Register of Legal Persons.

A foreign legal entity (founder) must also provide its registration certificate, its articles of association and the decision to establish a company in Lithuania. These documents must be legalised by the competent authorities in the foreign country.

Registration of a company takes seven days after all the necessary documents are duly executed and submitted to the Register of Legal Persons.

UABs must have at least one and less than 250 shareholders. There are no restrictions in respect of the number of shareholders in an AB. The shareholders may be resident or non-resident, legal entities or natural persons.

The minimum authorised (share) capital is LTL 10,000 (approximately EUR 2,900) for UABs and LTL 150,000 (approximately EUR 43,500) for ABs. One fourth of the authorised (share) capital must be monetary contributions; however, such monetary contributions may not be less than the minimum of LTL 10,000 for UABs and LTL 37,500 for ABs. The remaining part of the contribution may be either monetary contribution or contribution in kind. Contributions in kind must be valued by a certified asset appraiser before registration of the company.

Share capital may be increased or reduced by a decision of at least two-thirds of the votes at a general shareholders' meeting. Reduction of the authorised (share) capital with the purpose to pay out funds to the shareholders can be decided at the annual general shareholders' meeting only and the funds must be paid out to the shareholders in cash within a period of 30 days subject to certain conditions to be met.

The company's equity must not be less than 50% of its authorised (share) capital.

## Management

The Lithuanian Company Law calls for the creation of a three-tier management structure, including the shareholders' meeting, the management board and the supervisory board. The latter two, however, are optional for private limited liability companies as the management structure of UABs may be limited to the shareholders' meeting and the

head of the company, i.e. formation of a supervisory council and/or board is not mandatory for UABs.

There are no requirements regarding the residency of members of managing bodies.

The shareholders' meeting is the supreme corporate body having exclusive powers to make decisions such as amending the articles of association, increasing or reducing the share capital, approving the annual financial statements, liquidation, reorganisation, etc. Decisions at the shareholders' meeting are made by a simple majority of votes present (i.e. 50% plus one vote), except for the most important decisions, e.g. increasing/reducing the share capital, approving the financial accounts, profit allocation, etc., which must be made by a qualified majority of votes of at least two-thirds, three-quarters or higher.

The company is managed and represented by the head of the company (managing director, president, etc.). Quantitative representation may also be established in the company. An employment contract must be concluded with the head of the company.

## **Branch of a foreign company**

A branch of a foreign company does not have the status of a legal person. The foreign company is fully liable for the obligations of its branch. The branch may carry out business activities, enter into contracts and assume obligations within the scope of the powers granted by the foreign company.

At least one of the persons representing the branch (e.g. branch manager) must reside in Lithuania.

The branch must register for corporate income tax in Lithuania. There is no branch tax imposed on branch earnings paid to the head office of a foreign company.

Banking and insurance services may also be rendered through branches opened in Lithuania.

Foreign banks may open branch or representative offices in Lithuania. Banks incorporated in other EU member states are entitled to carry out financial activities based on the freedom of services if they have been granted an appropriate permission to carry out such activity in the country where they have a registered office.

Domestic insurance companies must have activity licenses issued by the Insurance Supervisory Authority for an unlimited period of time. A license for insurance activity is effective in all other EU member states, providing the insurance activities are carried out through exercising the right of establishment and/or the right to provide services.

In order to carry out insurance activities in Lithuania, foreign insurance companies must have licenses issued in their home countries as well as permissions from the competent authorities of these foreign countries to carry out their activities in Lithuania.

## Representative offices

Foreign companies may establish a representative office for representational and promotional purposes.

A representative office is a subdivision of a legal entity having its legal seat in Lithuania. A representative office is entitled to perform limited business activity only. The representative office does not have the status of a legal person. The foreign company is fully liable for the obligations of its representative office.

There is no requirement to have a separate balance sheet for a representative office. If activity carried by a representative office exceeds that permitted, such activity will become subject to profit tax in Lithuania.

At least one person acting on behalf of the representative office (e.g. manager of the representative office) must reside in Lithuania.

Representative offices are to be registered with the Register of Legal Persons.

## Mergers

Mergers are regulated under the Lithuanian Civil Code. The Company Law also establishes mandatory requirements for mergers of ABs and UABs.

A merger is an acquisition in which all assets and liabilities are absorbed by the acquiring entity and can be performed in two different ways:

- One (or more) existing company is merged with another existing company so that all rights and obligations of one company are transferred to another and the company ceasing to exist is deregistered from the Register of Legal Persons without liquidation procedures
- Two (or more) existing companies are merged into a new legal entity so that all rights and obligations of the companies participating in the merger are transferred to the newly established legal entity and those existing companies are de-registered from the Register of Legal Persons without liquidation procedures. This type of merger includes formation of a new company.

A company may participate in a merger only after its statutory capital has been fully paid up. The decision on a merger must be adopted by the General Meetings at least 30 days after the public announcement on the prepared merger terms.

Companies in a merger must publicly announce the merger conditions three times with at least 30-day intervals or provide an announcement once and notify all the companies' creditors in writing.

The assets, rights and obligations of the companies in a merger are assigned in accordance with the merger terms approved by the general shareholders' meetings of all companies participating in the merger.

## **Cross-border mergers**

Cross-border mergers may also be implemented in Lithuania. Lithuania has fully implemented the Directive of the European Parliament and of the Council of 26 October 2005 on cross-border mergers of limited liability companies. A cross-border merger may be an option when considering the minimisation of administration costs and the scope of reporting requirements mandated in each country where group business activity is carried out.

In order to facilitate cross-border merger operations, each company participating in a cross-border merger remains subject to the provisions and formalities of the national law which are applicable in case of national merger.

Only limited liability companies of the same legal type can participate in a cross-border merger.

Common draft terms must be drawn up for all companies participating in a cross-border merger. These terms must be publicised for each merging company through an entry in the appropriate public register.

The employees of the merging companies are vested with certain participation rights which are subject to regulations set in the national laws.

## **Going public**

Only public limited liability companies (AB's) enjoy the opportunities to go public in Lithuania.

The Vilnius stock exchange (VSE) is the sole operator of the regulated market in Lithuania. The VSE organises trading in financial instruments on the following lists: the Main list, Secondary list, Debt Securities list and Fund list. The financial instruments to be admitted to the trading lists must have no restrictions to their transfer, must be freely negotiable, entitling equal rights and fully paid up. A prospectus of the financial instruments must be approved and published.

There are special requirements set for the issuers and shares regarding admission into a particular list. For example, an issuer intending to enter the Main list must have been operating actively for the preceding three years. The projected capitalisation of shares or the capital and reserves of the company must be not less than EUR 4 million during the preceding financial year. Prior to admission to the Main list a sufficient portion of free

float must be public after distribution in Lithuania and/or one of the other EU member states.

An issuer seeking admission of its financial instruments to a list must file an application with the VSE. The Management Board of the VSE must pass a decision concerning admission to the Main list within six months from the date of receipt of the application. The term for other lists is three months.

Decisions on admission to the list are passed provided the financial instrument and their issuers satisfy the requirements set by the applicable laws. The stock exchange regulations are based on the provisions of the EU legislation.

## **Insolvency proceedings**

A company is considered to be insolvent if it fails to settle with creditors (e.g. does not pay its debts, fails to perform work which has been paid up in advance, etc.), and the overdue obligations/debts exceed half of the value of the company's assets recorded in the balance sheet. Bankruptcy proceedings of companies may be initiated by the court or by the creditors, owners or the management of the company. The proceeding initiated by the court are deemed a judicial proceeding and the one initiated by the creditors, a non-judicial (extrajudicial) bankruptcy procedure.

A petition for bankruptcy with the court may be filed if at least one of the following conditions occurs:

- a company fails to pay remuneration and other employment-related amounts when due
- a company fails to pay for goods received, work performed, services rendered, or defaults in the repayment of loans, or does not fulfil other contractual obligations
- a company fails to pay due taxes or other compulsory contributions prescribed by law
- a company has made a public announcement or notified its creditors in any other manner of its inability or lack of intent to discharge its obligations
- a company has no assets or income to settle its debts and therefore a court bailiff has returned the writs of execution to a creditor.

The court is entitled to call current and previous management and accountants of the company to give their explanations and documents related to the bankruptcy case. Ex-management and bookkeeping personnel can be called if their employment with the company terminated less than 12 months prior to the initiation of the bankruptcy proceeding.

The court has a right to restrict a person's right to become manager of a public and/or private entity for 3-5 years if the person has breached obligations mandated according to the regulations set in bankruptcy laws.



A simplified judicial proceeding can be arranged in case a company has no assets or the value of the assets is insufficient to settle the costs for the court proceedings and bankruptcy administration.

Creditors intending to file a bankruptcy petition to the court must give a prior written notification to the company concerned about their intention. Among other things the creditors must allow the company a period which cannot be shorter than 30 days in which the company may settle with creditors. Upon expiry of this period, the creditors can apply to the court if the company fails to settle.

Non-judicial bankruptcy proceedings can be initiated if there are no proprietary claims filed in courts, including those related to labour relationships, and if no compulsory collection of debts is applied to the company. Creditors' meeting shall be convened in order to obtain consent to start non-judicial bankruptcy proceedings. Decision to start non-judicial bankruptcy proceedings may be adopted if the creditors having claims equal to at least four-fifths of the company's total liabilities vote for it.

Specific features of the bankruptcy process of banks, credit unions, insurance companies, agricultural enterprises, intermediaries of public trading in securities and other enterprises may be established by other laws regulating the activities of the said enterprises and public agencies.

The Lithuanian Criminal Code establishes criminal liability to a person, whose wilful wrong management of the company caused bankruptcy and this resulted in major material damage to the creditors. The liable person may receive a penalty of up to three years' imprisonment.

## Chapter 3

# Business Taxation

## Estonia

### **Tax residency**

A legal person is considered as an Estonian resident if residency is established under Estonian law. European public limited companies (SE) and European associations (SCE) whose seat is registered in Estonia are also residents.

### **Corporate income tax**

#### **Tax rates**

The profits earned and retained in a company are not subject to taxation. The income tax rate on gross dividends is 21% (in 2009), although the tax is calculated on the net amount of dividends by applying a tax rate of 21/79. Thus a company not distributing profit is not obliged to pay income tax. Taxable expenses and payments are taxed at the rate of 21/79 as well.

#### **Taxable persons**

The principles for taxation of income of resident companies, incorporated companies, branch offices and permanent establishments of foreign companies have stayed the same since the year 2000.

Branch offices and permanent establishments are subject to tax on transfer of income earned in Estonia.

## Tax base

A conceptual difference compared to the classical income tax system is that, instead of taxing the profit of resident legal persons and registered permanent establishments, the distribution of profits (as well as transactions that can be treated as hidden distribution of profits) are taxed. Income taxation has shifted from earning profits to the distribution of profits. The term "distribution" is treated more broadly than just direct dividend payment. It also includes hidden profit distributions and certain expenses, which can be considered profit allocation, e.g. fringe benefits, gifts, donations, and expenses and payments unrelated to business.

As of 2009 the tax base of a resident company also includes payments made upon reduction of share capital or contributions, or redemption or return of shares or contributions, but also upon other payments made from equity or upon payment of liquidation proceeds. In that case, a resident company will pay corporate income tax on the amount in which the abovementioned payments exceed monetary and non-monetary contributions made to the company's equity.

The Income Tax Act has been changed several times since 2000. Therefore, upon distribution of dividends or other payments made from the company's equity it is important to observe when the profit was earned and distributed to apply taxation according to the wording of the Income Tax Act that was in effect at the time.

## Inter-company dividends

From 2000 until 2003, Estonian companies paid income tax on distribution of dividends to natural persons, certain non-profit organisations and non-residents. Distribution of dividends was not taxable when the dividends were paid to other resident companies or to permanent establishments registered in Estonia. Since 2004, income tax must be paid on profit distributions regardless of the recipient.

Companies that distribute dividends from retained earnings from periods prior to the year 2000 may deduct the income tax paid on these retained earnings from the dividend income tax. If a company made no profit prior to the year 2000, it will not be able to reduce tax liability, even if profit is made in the future years.

Before 2005, the tax credit system applied to dividends received from abroad, if the same dividends were redistributed by an Estonian company. In 2005 the credit method was replaced with the exemption method. The dividends received by an Estonian company from abroad are not taxable in Estonia in the case of redistribution of these profits if the dividend was received from an EEA or Swiss resident company or if income tax was paid or withheld on these dividends abroad (except from low tax territory) and the Estonian company owned, at the time of receiving the dividends, at least 10% (20% from 2005 until 2006, 15% from 2007 until 2008) of the shares or votes in the subsidiary.

As of 2009, the tax base has been broadened. For that reason, the tax exemption on dividends is now applied also to dividends the basis of which is a payment that was received upon reduction of the share capital or contributions, or redemption or return of shares or contributions, but also upon other payments received from equity or upon receipt of liquidation proceeds if the payment or the share of profit that serves as the basis of the payment has been subject to taxation and the Estonian company owned at least a 10% holding in the subsidiary.

The exemption is applied also to payments made from equity of a company or upon payment of liquidation proceeds if the basis of the payment is a dividend, payment from equity or liquidation proceeds that corresponds to the same conditions as in the case of dividends that are exempt from further taxation.

If the conditions for the application of an exemption method are not fulfilled, the credit method is generally applied.

### **Gifts, donations and representation costs**

A resident company pays income tax on gifts and donations made to natural persons and non-residents, non-profit organisations not included in the list approved by the government and resident business undertakings.

Payments made for expenses incurred while receiving guests and business partners (accommodation, catering, transportation and cultural expenses) are also taxable if they exceed the limits which are dependent on the payroll.

### **Fringe benefits**

Fringe benefits are taxable at the level of an employer with income tax at the rate of 21/79 and social tax at the rate of 33% (the income tax amount is also subject to the social tax). All benefits granted to employees, including the members of management and supervisory boards, the self-employed who has been providing services or selling goods to the employer, or the individual having other contractual relationship with the company, also to the husband, parent or child of the employee, are taxed as fringe benefits.

### **Reserves and provisions**

Companies may establish reserves without tax consequences.

### **Tax losses**

Losses have no effect on corporate taxation.

## Capital gains

Capital gains are not taxed separately, but are included in profits subject to corporate income tax upon distribution. Thus, the capital gains received by an Estonian company are not taxable as income, but become subject to taxation upon distribution.

## Groups of companies

Companies forming a corporate group are treated as individual companies for tax purposes. Thus, there is no fiscal unity or similar concept in Estonian income tax legislation.

## Thin capitalisation

There are currently no thin capitalisation regulations in Estonia.

## Transfer pricing

If the value of a transaction conducted between associated persons (including transactions carried out between a permanent establishment and its head office) differs from the value of a similar transactions conducted between independent persons, the tax administrator may, upon making an assessment of income tax, apply the value of transactions used by independent persons under similar conditions. As of 1 January 2007, the transfer pricing regulation is applied to the transactions carried out between related resident companies in the same way as it was applied before to the transactions carried out between related non-residents or an individual.

In 2007, the new wording of the Income Tax Act imposed on companies the obligation of documenting their transactions with associated parties.

## Tax collection

A legal person has the obligation to file an income tax return for the period of taxation (calendar month) by the 10th day of the month following the taxation period. VAT registered taxpayers must submit a tax return regardless of whether any events resulting in tax obligations have occurred. Income tax is to be transferred to the tax authorities by the same date.

Foreign branches and permanent establishments must file an annual report with the tax administrator no later than six months after the end of the financial period if the annual report does not have to be submitted to the Commercial Register.

## Withholding taxes

Domestic withholding income tax rates for payments to non-residents (both entities and individuals) are as follows:

- payments from services provided in Estonia – 10%;
- royalties – 0% or 10%; the 0% rate is applied if royalties are paid at the market price between associated companies established in the European Union. In all other cases - 10% is applied;
- interest – 0%, however, 21% income tax is withheld from the portion of interest that significantly exceeds the market value;
- rental payments – 21%.

There is no withholding tax on dividends.

## Value added tax

### Tax base

Taxable transactions are the supply of goods and provision of services, if made in Estonia. The tax base also includes certain actions carried out for no consideration, e. g. the giving of business gifts and the private use of business assets.

### VAT payers

If an Estonian entity (including the permanent establishment of a foreign person) makes taxable supplies in Estonia over the VAT registration threshold (EEK 250,000 - approximately EUR 16,000), it is required to register and account for Estonian VAT. Taxpayers with annual sales less than EEK 250,000 are not liable for VAT. If an entity trades below the registration threshold it can still choose to register voluntarily for VAT. However, no registration is required if the taxable supplies consist of only zero-rated supplies, except the intra-community supply of goods.

When a trader, with no permanent establishment (PE) in Estonia and liable for taxation in another country, makes a taxable supply in Estonia that is not taxed by the Estonian taxable person upon acquiring the goods or services, then that foreign trader must register for VAT from the date the taxable supply was made. It follows that no registration threshold applies for such traders. Different rules apply in the case of distance sales and e-commerce.

If a business is not registered for VAT in Estonia but sells and delivers goods from another EU member state to customers in Estonia who are not VAT registered ("distance sales"), where the value of those sales exceeds a threshold of EEK 550,000, a business is required to register and account for VAT in Estonia.

## VAT rates

The standard rate of VAT is 20%.

There is a reduced rate of 9% for certain goods and services, including:

- books and most periodicals
- medicines
- medical equipment for the personal use of the disabled
- accommodation services.

There is an extensive list of zero rate supplies, including:

- international transport services
- exports
- supply of aircraft operating on international routes
- supply of sea-going vessels for navigation on the high seas
- supplies carried out through a free zone
- supplies effected in the customs and tax warehouse.

If an Estonian company supplies services to a VAT registered customer in another EU Member State or a customer (business or private) outside of the EU, then it can zero rate supply provided the service falls within one of the following categories.

- granting of the use of intellectual property or transferring of the right to use intellectual property
- advertising services
- consulting, engineering, legal, accounting, auditing and translating services, as well as data processing and the supplying of information
- banking, financial and insurance transactions including reinsurance but excluding the hire of safes
- the supply of staff
- the hiring out of movable tangible property with the exception of all forms of transport
- telecommunication services and radio and television broadcasting services
- electronically supplied services
- services of an intermediary.

## Exemptions

The list of exemptions includes:

- immovable property or parts thereof (there is an option to tax the sale of immovable property if the tax authorities are informed beforehand)
- the leasing or letting of or establishment of a usufruct on immovable property or parts thereof (an option to tax)
- insurance and financial services (an option to tax financial services)
- securities
- betting, gaming, and lotteries
- education
- health and welfare services
- postal services and postal stamps
- investment gold.

## Limitations to input VAT

There are certain items that a person cannot recover VAT on. For example:

- exempt supplies: where VAT relates to both taxable and exempt supplies, an apportionment is required
- non-business (including private) activities: where VAT relates to both business and non-business activities, an apportionment is required.
- business entertainment and payment for goods or services relating to the provision of meals or accommodation for employees or guests; however, VAT can be recovered on the accommodation during a business trip
- purchases falling within the "Tour Operators' Margin Scheme"; the VAT on goods and services which fall under this scheme cannot be reclaimed
- goods sold under one of the margin schemes for second hand goods, all other similar schemes which provide for VAT to be accounted for on the goods' sales margin, but do not allow VAT recovery on the purchase of those goods.

## Irregularities

According to the Estonian VAT Act, a reverse charge is applied in the case of acquisition of goods or receipt of services from a foreign taxable person who is not registered as a taxable person in Estonia. Therefore, if a foreign trader supplies goods or services to an Estonian taxable person, then a VAT registration is not mandatory in Estonia, provided the Estonian person applies a reverse charge on acquired goods or services.



Estonia applies a VAT registration threshold for small and medium sized enterprises whose annual turnover is lower than EEK 250,000 (EUR 16,000).

## Excise duties

The Estonian excise legislation is based on the excise legislation of the European Union. The excise is imposed on:

- Alcohol
- Tobacco
- Fuel
- Electricity
- Packaging
- Natural gas
- Oil shale

Excise duty is charged on fuel that is produced in Estonia, which has been brought into Estonia from another member state and the fuel that is declared for free circulation in Estonia. Estonia obtained permission from the EU to exempt bio fuels from excise from August 2005 and the exemption is applicable for a period of 6 years (up to 2011).

Excise duty is imposed on tobacco products (smoking tobacco, cigarettes, cigars, cigarillos, chewing tobacco) produced in Estonia or brought into Estonia. Distribution of tobacco products without tax stamps is prohibited.

Excise duty is imposed on wine, beer, fermented beverages, intermediate products and other alcohol produced in Estonia or brought into Estonia. Alcoholic beverages with ethanol content above 22% volume, whose packaging containers hold over 0.2 litres, or if the excise duty amount constitutes more than 10 EEK, must be revenue stamped.

Excise duty on packaging is imposed on packaging filled in Estonia, acquired from another Member State or imported to Estonia. The payers of excise duty, who do not meet the recovery rates of packaging, should pay excise duty for the quantity of the packaging unused. Excise duty is paid by the importer of packages, by the user of packages or by the person who acquired packaging from another Member State upon the sale, exchange, free transfer or use for self-consumption of packaging.

The obligation to pay excise duty on electricity applies to the network operators who are engaged in the provision of network services through a network.

Excise-able goods can be received from another Member State under the excise duty suspension arrangement if the recipient is an excise warehouse keeper or a registered trader.

Excise duty is administered by the Estonian Tax and Customs Board.

## **Real estate tax, land tax**

The only property tax imposed in Estonia is land tax. In general the annual tax rate is between 0.1% and 2.5% of the taxable value of the land, which is determined according to provisions of the Law on Land Value. Most land is subject to tax. The owner of the land is obliged to pay the tax.

## **Other (*local taxes*)**

Tax on trucks heavier than 12 tonnes has been in effect since the beginning of 2004.

### **Local taxes**

Local municipalities are entitled to establish their own taxes based on the Law on Local Taxes. Commonly established local taxes are: advertising tax, tax on the closing of streets and roads, sales tax and parking tax.

# Latvia

## **Tax residency**

The criteria for establishing a company's residence for tax purposes is its incorporation in Latvia or that it legally should have been registered as a tax payer in Latvia, as in the case of a permanent establishment. Latvia does not have an effective place of management test of residence.

Taxable entities are resident companies (but not partnerships) and non-resident entities as well as permanent establishments of non-residents and non-resident entities which derive income from a Latvian source.

## **Corporate income tax**

### **Tax rates**

Latvian corporate income tax is charged at a rate of 15%.

Companies registered in Special Economic Zones eligible for specific tax rate reductions will continue to calculate their reduction based on the historic tax rate of 25%.

## Taxable persons

Latvia has a self-assessment taxation system. The taxpayer calculates the amount of tax payable and reports this amount in a declaration. The taxation authorities may audit the declaration within a period of 3 years after the due date for filing the tax return for the year in question.

## Taxable base

The taxable base of resident companies is their worldwide income and capital gains. A permanent establishment (branch) of a non-resident company is treated as a separate Latvian taxpayer. The profits of a Latvian branch of a non-resident company are taxed on a normal basis at the same rate as the profits of a resident company. However, internal charges between the Branch and its Head Office such as interest, management fees, etc. are not deductible. Head office costs attributable or allocable to the branch may be deducted.

Companies registered in Latvia that operate ships internationally have the option of paying corporate income tax based on the tonnage of the individual vessels used in their operations. Once this option is chosen it must be continued for 10 years.

## Inter-company dividends

Regardless of the level of ownership, dividends received from Latvian companies are tax exempt except for dividends paid by a Latvian company which utilises some form of corporate income tax relief. In this case, the dividends are subject to tax according to the percentage of tax relief received by the paying company.

Dividends from non-resident companies are normally taxable. However, they are not taxable if dividends are received from companies registered in the EU or in EEA countries.

## Gift and donation costs

A resident company may not receive corporate income tax deductions for gifts and donations made to individuals and non-residents, non-profit organisations and resident business undertakings. However, a company may receive a tax payment discount of 85% of the amount of donation made to public benefit organizations that are registered with the Ministry of Finance.

## Fringe benefits

All benefits provided to employees, including the members of management and supervisory boards, self employed individuals who have been providing services or selling goods to the employer or an individual having other contractual relationships with the company, as well as to the husband, parent or child of the employee, are taxed as fringe benefits.

Fringe benefits are taxable according to the same principles as salary paid to employees –with personal income tax of 23%, employee social tax of 9% and employer’s social tax of 24.09% in addition to the gross salary.

### Reserves and provisions

Reserves and provisions are not deductible, except for banks and insurance companies in specific circumstances.

### Tax losses

It is possible to carry tax losses forward up to 8 years. Where a change in the "control" of a company occurs, the right to existing losses is lost unless the company continues to undertake for the next five years the same fundamental business activity that it undertook during the previous two years. Companies are not allowed to carry losses back. Taxpayers registered in Special Economic Zones have a 10-year carry forward limit.

### Capital gains

Capital gains are not taxed separately, but are included in profits subject to corporate income tax.

### Groups of companies

A parent and subsidiary(s) that have 90% common ownership are treated as a group. The companies must be Latvian, other EU country or EEA country residents, or residents of a country with which Latvia has a Double Taxation Treaty. Although there is no fiscal unity for taxation purposes, consolidated financial statements are required for groups. Losses can be transferred between Latvian resident group members and under certain circumstances, with EU and EEA countries residents.

### Thin capitalisation

Interest payments may be deducted from the company's taxable income; however, the deductible amount is restricted. There are no deduction restrictions if the interest is paid to a Latvian resident or an EU registered credit institution. For the reasons of preventing discrimination, this provision can also be applied to interest payments for the funds borrowed from a country with which Latvia has concluded a Double Tax Treaty.

According to the thin capitalisation rules, two calculations for determining the deductible amount of interest must be made. The calculation of deductible interest must be done on an annual basis.

Under the first calculation, the amount of principal upon which interest was paid during the year is multiplied by 1.2 times the average short-term interest rate for the last month of the taxation period as determined by the Central Statistical Bureau of Latvia.

If the interest payment for the tax year exceeds this amount the excess is not deductible for taxation purposes.

Under the second calculation, the amount of interest paid is disallowed proportionally to the amount by which the average amount of the principal outstanding during the year exceeds a multiple of four times the company's equity as stated in its annual accounts at the beginning of the year, reduced by any amounts that are long term investment revaluation reserves or other reserves that have not been reflected in the profit and loss statement. Interest on "profit participating loans" is deductible with the same limits.

The higher disallowance is applied.

Non deducted interest payments cannot be carried forward for deduction in future taxation years. Taxable income can be reduced for a conditional loan interest amount that would be payable for a conditional loan in the amount by which equity has increased as a result of retained earnings.

### Transfer pricing

An arm's length price must be applied to transactions with associated foreign entities and also with resident companies which enjoy income tax relief.

### Tax collection

The tax period is the same as the fiscal year and may be different from a calendar year. An annual tax return must be filed within four months of the end of the tax period to which it relates. Large companies are allowed to extend this deadline up to seven months. Monthly advance payments of tax are required.

### Increase of asset value for depreciation for tax purposes

Tax depreciation for new technological equipment acquired between 2009 and 2013 will be calculated by multiplying the asset value with an increased ratio of 1.5.

### Withholding taxes

Domestic rates of withholding tax on payments to non-resident legal entities are as follows:

- dividends: 10%, except EU and EEA resident shareholders
- management and consulting fees: 10%
- interest to associated persons: 5-10%
- leasing payments: 5%

- rights to use intellectual property in respect of literature and artistic works: 15% (5% tax applies if the recipient is resident of another EU country and it owns more than 25% of the company paying interest)
- right to use other intellectual property rights: 5%
- payments for the use of fixed or movable property in Latvia: 5%
- payment for the sale of real estate located in Latvia: 2% of the total proceeds.

Corporate income tax of 15% must be withheld at source on any payments made to entities registered in or located in one of the low or zero tax countries and territories designated by the Latvian Government. The tax authorities may exempt payments from this requirement if certain conditions are met.

Excluded from the above are dividend payments, normal deposit interest paid by Latvian Credit Institutions and payments for goods that have their origin in a low or zero tax country or territory.

### Tax treaties

Foreign taxes paid are not tax deductible in Latvia. A tax credit may be granted for these taxes but not exceeding the amount of Latvian tax payable on that income (i.e. ordinary credit) on a source-by-source basis.

### Tax incentives and concessions

A company registered and operating in a special economic zone enjoys higher rates of depreciation and a longer term (10 years) for carrying losses forward. Companies registered and operating in a special economic zone may qualify for both immovable property tax relief of up to 100% and corporate income tax relief of 80%. Granted relief is subject to certain limits.

The following are other corporate income tax relief or concessions that are available:

- tax relief for tax paid in foreign countries
- tax relief for enterprises engaged in agricultural activity
- tax relief for charitable donations.

## Value added tax

### Tax base

Taxable transactions are the supply of goods or services within Latvia, self-consumption, the import of goods and export of goods and services and whose taxable transactions exceed LVL 10,000 in a 12 month period must register as a VAT payer.

### VAT payers

Individuals or legal entities that in the course of a trade or profession perform taxable transactions within Latvia.

### VAT rates

The standard VAT rate is 21%.

The following are examples of transactions subject to a VAT rate of zero (0):

- export of goods and intra community supplies
- transportation of export, import and transit goods
- services that are directly related to goods that are imported from third countries and are not released for free circulation within the EU that are rendered within a free zone territory or customs warehouse
- services where the place of supply is deemed not to be within Latvia
- supplies of goods and services connected with international transport and rescue ships
- international passenger traffic
- supplies of goods and services under diplomatic and consular arrangements.

The following are examples of transactions subject to a VAT rate of 10%:

- supply of listed medicines, medical goods and equipment
- supply of listed infant products
- supply of mass media products (only for printed media; from 2010 –standard rate)
- public transport services within Latvia
- supply of heating to inhabitants
- supply of electricity to inhabitants
- supply of gas to inhabitants, except for use of natural gas in motor vehicles

## Exemptions

The following are examples of VAT exempt transactions:

- transactions in shares and other securities
- banking and financial services excluding hire of safes and encashment
- insurance transactions
- the services related to welfare and social security work
- the provision of medical care
- education services
- sale of real estate excluding the first sale of 'new' buildings
- rental of domestic apartments to individuals
- betting, lotteries and other forms of gambling.

## Limitations to input VAT

There are certain items on which a person cannot recover VAT.. For example:

- exempt supplies: where VAT relates to both taxable and exempt supplies, an apportionment is required
- non-business (including private) activities: where VAT relates to both business and non-business activities, an apportionment is required
- business entertainment and payment for goods or services relating to the provision of meals or accommodation for employees; however, VAT can be recovered on accommodation during business trips
- expenses of a representative nature; 40% of the VAT is not recoverable.

Input VAT cannot be claimed in respect of exempt transactions and input VAT can only be claimed in respect of transactions that are directly related to the income generation of the individual or entity.

Latvian VAT legislation is in compliance with the EU 6th Directive.

## Excise duties

Excise duties are payable by producers or importers of:

- spirits and alcohol
- beer with an alcohol content exceeding 0.5% by volume



- certain tobacco products
- petroleum products
- soft drinks and coffee.

## **Real estate tax, land tax**

Tax on immovable property (land and buildings) is paid by individuals and legal entities that own or have legal control over real estate. The immovable property tax rate is 1% of the cadastral value. After the updating process of cadastral values during 2008 to 2010, the increase in the calculated tax amount, if the purpose of use of the real-estate is not changed, is limited to a maximum of 25% of the tax amount in prior year.

## **Other (*local taxes*)**

### **Natural resource tax**

The natural resource tax is imposed on:

- natural resources extracted over a licensed amount
- environmental pollution that exceeds a set limit
- goods injurious to the environment
- the packaging of imported and domestically produced goods.

# Lithuania

## **Tax residency**

A legal person is considered as a Lithuanian tax resident if it is established pursuant to Lithuanian law.

## **Corporate income tax**

### **Tax rates**

The general corporate income tax rate is 20%.

The 13% corporate income tax rate applies for:

- the taxable profit if an entity's average number of employees does not exceed 10 and income does not exceed LTL 500,000 (ca EUR 144,800) (certain exemptions apply)

The 0% corporate income tax rate may be applied for:

- social companies with more than 40% of their employees being disabled, long-term unemployed, and other supported social groups (additional requirements apply)
- companies established in the Free Economic Zone if their investments exceed EUR 1 million (for 6 periods, a 0% rate is applied, for the 10 following periods – 50% of the standard rate)
- production companies with more than 50% of their employees with limited working ability. If the fraction of employees with limited working ability is lower, then a partial deduction of corporate income tax is given.

Further requirements have to be fulfilled by the above mentioned companies in order to be eligible for the incentives.

If an entity's average number of employees does not exceed 10 and the turnover does not exceed LTL 1,000,000 (approximately EUR 289,600), the amount of LTL 25,000 (EUR 7,240) shall be taxed at 0%, the remainder by 20% (certain exemptions apply).

## Taxable persons

Lithuanian and foreign taxable entities are considered as corporate taxpayers.

Lithuanian taxable entities are defined as all types of entities, registered in Lithuania and having the status of a legal person.

Foreign taxable entities are all types of entities, domiciled in a foreign country and incorporated under foreign laws. In respect of foreign tax payers, the entity is not required to bear legal person status.

## Tax base

Lithuanian entities are subject to corporate income tax on their world-wide income.

The tax liability of foreign units is limited to income sourced in Lithuania, including income earned through permanent establishments.

A foreign unit is deemed to have a permanent establishment in Lithuania if it meets any of the following criteria:

- it performs activities on a permanent basis, or
- it performs activities through a dependent representative (agent), or
- it uses a construction territory, construction, assembling or equipment object, or

- it uses equipment or construction including boreholes and ships for investigation and the extraction of natural resources.

A foreign company is deemed to be engaged in permanent commercial-business activities in Lithuania, leading to a permanent establishment, if the activities are carried out for longer than six months and normally there is a completed cycle of commercial activities.

Permanent establishments of foreign entities must be registered with the local tax authorities and non-registration does not provide release from payment of Lithuanian corporate income tax.

When calculating the taxable profit of a Lithuanian or foreign taxable entity, the following amounts are deducted from income: (1) tax exempt income; (2) allowable deductions and partly allowable deductions.

Tax exempt income includes:

- the gain from sales of shares, received from an EU company or a company registered in a country with which Lithuania has the double tax treaty (participation requirement: 25% for at least 2 years)
- received insurance payments (not exceeding damages)
- proceeds of a bankrupted company, received from the disposal of its assets
- revaluation of the fixed assets and liabilities, except revaluation of financial derivatives for hedging purposes
- received penalties and fines, etc.

Furthermore, certain types of income for insurance and investment companies are also exempt.

Allowable deductions are all costs actually incurred which are usual for the activities of the entity and are necessary for the earning of its income or the gaining of economic benefit, unless the law establishes otherwise.

Partly allowable deductions, which may be tax-deductible subject to certain requirements, include the following:

- depreciation and amortisation of fixed assets
- maintenance, repair and reconstruction of fixed assets (except for cases when such maintenance, repair or reconstruction prolongs the useful lifetime of the fixed assets)
- business trips
- advertising and entertainment
- ordinary loss of inventories

- taxes
- bad debts
- payments to the benefit of employees
- provisions of credit institutions and insurance companies
- granted support
- membership fees
- tax losses.

The main types of non-deductible expenses are as follows:

- penalties and default interest
- interest and other payments related to the obligations of related parties
- compensation for damages
- dividends and other profit distributions
- expenses of purchased goods (services) from tax haven entities, if these goods (services) are not paid for more than 18 months
- payments to tax haven entities if a Lithuanian entity does not prove that these payments are related to the ordinary activities of tax haven entities.

## Dividends

Dividends paid by a Lithuanian company to a foreign company holding not less than 10% of the shares granting the same percentage of votes not less than 12 months are tax free, except for dividends paid to tax haven countries. In other cases, dividends are subject to 20% withholding tax.

## Tax losses

Tax losses (except for losses from the disposal of securities or financial derivatives) can be carried forward for an unlimited time period if the economic activity from which the loss originated is continued. Losses from the disposal of securities or financial derivatives can be carried forward for 5 years and exclusively to offset gains from the disposal of securities or financial derivatives.

Tax losses may not be carried back.

## Capital gains

Capital gains earned by Lithuanian entities are included in taxable income for income tax purposes. Capital gains are taxed at a general 20% tax rate, unless a 13% rate may be applied due to the limited number of employees and income of the company.

## Groups of companies

A group of companies is a group consisting of the parent company and associated entity (entities), where the parent company possesses not less than 25% of the shares.

Neither group consolidation nor transfer of losses within the group company is possible for corporate income tax purposes.

## Thin capitalisation

A certain part of interest paid to a controlling lender may not be deductible for profit (corporate income) tax purposes.

The aforementioned controlling borrower includes both a resident and a non-resident shareholder and is deemed to be as such if the following criteria are met:

- the shareholder controls a Lithuanian entity on the last day of a taxable period, and
- the shareholder (in)directly owns more than 50% of the shares in a Lithuanian entity, or
- the shareholder together with related parties owns more than 50% of the shares in a Lithuanian entity and the part owned by this shareholder is not less than 10%.

The non-deductible part shall be calculated based on the debt/equity ratio of 4:1, i.e. interest related to the debt exceeding this ratio shall be non-deductible for profit (corporate income) tax purposes. It should be noted that these rules are applicable even if withholding tax on interest is paid.

In addition to interest expenses, these rules are also applicable to other expenses related to the debt exceeding the ratio of 4:1, e.g. currency exchange losses.

Thin capitalisation rules may be avoided when a Lithuanian entity proves that the same loan under the same terms would be available between independent persons.

## Transfer pricing

In general, transfer pricing provisions are adopted in the Law on Profit (Corporate Income) Tax, the Law on Individual Income Tax and the Law on Value Added Tax with their effect as of 1 January 2004. The transfer pricing provisions are harmonised with the OECD Transfer Pricing Guidelines for Multinational Enterprises and Tax Administrations.

The following five transfer pricing methods can be used in order to be in compliance with the arm's length principle:

- Comparable uncontrolled price method

- Resale price method
- Cost plus method
- Profit split method
- Transactional net margin method

The comparable uncontrolled price method must be used first. When not enough data is available, the resale price or cost plus methods should be used. The profit split and transactional net margin methods have the lowest priority and can be used provided that the data is not sufficient to apply the first three methods.

### Documentation requirements

The obligation to produce a written transfer pricing documentation applies to companies meeting at least one of the following criteria:

- sales income of the entity before the taxable year when the transaction was actually carried out, exceeded LTL 10 million (approximately EUR 2.9 million)
- financial companies and credit institutions
- insurance companies
- foreign entities, engaged in activities through permanent establishments, if their foreign entities' attributable income exceeds LTL 10 million (approximately EUR 2.9 million) before the taxable year when the transaction was actually carried out.

Transfer pricing documentation must be filed with the tax administrator within 30 days after the request. Tax payers should provide the transfer pricing documentation in its original language if it is not available in the Lithuanian language. The tax administrator may require translation of these documents into Lithuanian, establishing a deadline for submission of the translation.

Transfer pricing documentation should be submitted in the original form, if it is sufficient for the identification of the reliability of the information without requiring extra evidence.

### Tax collection

Annual corporate income tax returns must be filed and corporate income tax must be paid within nine months after the end of a taxable period. Corporate income tax must be paid in advance instalments based on the result of the previous taxable period. Newly registered companies are exempt from advance payments for their first year of operation.

Withholding tax returns must be filed within 15 days after the end of the month when the taxable payment was made to a foreign entity. If the tax is not withheld from the payment made abroad and it is paid from Lithuanian payer's funds, the withholding tax cost is not deductible for corporate income tax purposes.

## Withholding taxes

The taxable income of foreign units which is subject to withholding taxes in Lithuania includes the following:

- interest
- authorship remuneration, license and know-how fees and other royalty payments
- income from the disposal or renting of real estate located in Lithuania
- income from profit distribution, including dividends.

A 20% withholding tax rate applies to the taxable income of foreign units received in Lithuania, except for interest and royalties.

A 10% withholding tax rate applies to interest and royalties.

The domestic withholding tax rate can be lowered under the tax treaties to which Lithuania is a party.

## Tax treaties

Currently, Lithuania has concluded tax treaties with 46 countries.

Lithuanian entities are entitled to deduct profit tax or similar taxes paid abroad from the corporate income tax payable in Lithuania. The deducted amount, however, may not exceed the amount of income tax payable in Lithuania on that type of income.

Special rules apply with respect to the income of controlled foreign companies, which is attributed to the taxable base of a Lithuanian entity.

## Tax incentives and concessions

Despite the fact that corporate income is taxed more heavily, there are plenty of tax incentives for companies. Tax relief is available for agricultural companies, free economic zone companies, manufacturing companies employing people with disabilities, social companies, and cooperatives. Corporate income tax relief may also be available for those companies initiating investment projects. Additionally, the income of investment companies with variable capital and insurance companies' income from investments (except for dividends) are exempt from corporate income tax. The government is implementing strategies to reduce the burden of bureaucracy for companies even after the World Bank's research has shown that Lithuania provides one of the easiest environments for starting and developing a business in the EU.

## Value added tax

The Lithuanian VAT system is made compliant with the VAT directive (2006/112/EC). The EC law provisions regarding VAT on intra-Community trade, triangulation and distance selling are implemented into national legislation.

### Tax base

VAT is applied to goods, supplies and rendering of services for consideration by taxable persons if such goods are supplied or services are rendered in Lithuania, as well as to goods imported into Lithuania or acquired of goods from another EU member state. The concept of taxable persons also includes foreign persons engaged in business activities in Lithuania.

Consulting, management, market research, supply of information, telecommunications, software, legal, audit, financial services and leasing of movable assets, etc., rendered to foreign entities, are not subject to Lithuanian VAT if they are rendered to persons from third countries or to VAT payers from other EU member states. If the buyer of such services is a Lithuanian person, VAT is levied under the "reverse-charge" mechanism, if the supplier is non-Lithuanian.

### VAT payers

Lithuanian persons whose income exceeds LTL 100,000 (approximately EUR 29,000) per annum should register as VAT payers. If the entity performs VAT exempt activities, it may apply for exemption from VAT registration.

Foreign persons should register for Lithuanian VAT if their activities in Lithuania are subject to VAT (except for cases where the obligation to account for VAT transfers to the purchaser or where the zero VAT rate applies). The threshold of LTL 100,000 (EUR 29,000) to foreign persons is not applicable.

Foreign persons must register for VAT in Lithuania through a fiscal agent unless they are incorporated in an EU member state - such persons can be registered as Lithuanian VAT payers directly.

### VAT rates

The standard VAT rate is 19%. The zero rate may be applicable in certain cases.

There is a compensation rate of 6% for supplies of goods and services made by farmers.

The 0% rate applies to exports outside the European Union, supplies of goods to another member state, supplies of gold to the system of Central Banks of European countries and the Central European Bank, goods and services intended for diplomatic missions, supplies to charities, supply, modification, modernisation, and the hiring of sea-going ships and aircraft.



## Exemptions

Goods and services related to health care, social and cultural services and sport, if they are produced/rendered by non-profit entities, as well as other services, including the supply of goods and the rendering of services for charity and support purposes, postal services, insurance services, financial services, leasing or dwelling and other immovable property, etc., are exempt from VAT (without deduction for input VAT).

## Limitations to input VAT

A VAT payer should have the right to deduct input (or import) VAT on goods/services, provided that the goods/services are intended for use in the following activities of the VAT payer:

- supply of goods/services on which VAT is chargeable
- supply of goods/services outside the territory of the country where such supply of goods/services would not be exempt from VAT if effected within the territory of the country; the above condition shall not apply with regards to the supply outside the territory of the country of insurance services and/or financial services.

In order to fully or partly deduct the input (or import) VAT, a VAT payer must possess documents providing that the supply may be considered as having taken place outside the territory of the country according to the criteria established by the Lithuanian VAT Law. If this is not proved, the supply shall be considered to have taken place within the territory of the country, and output VAT must be settled.

A VAT payer has a right to deduct input VAT on the goods/services acquired (or imported) prior to the day of its registration as a VAT payer, provided that they will be used for VAT taxable activities.

Input VAT should be deducted only in the case where a VAT payer holds an appropriate invoice. This amount of VAT must be specified in the invoice held, and the VAT payer must be indicated as the purchaser of the goods/services.

## Excise duties

Excise duties are levied on production in, or import into Lithuania of the following items:

- ethyl alcohol and alcoholic beverages
- tobacco products
- fuel
- electricity.

Importers and producers are liable to pay excise duties to the state budget.

## Real estate tax, land tax

Real estate located in Lithuania, except for land, is subject to real estate tax.

The real estate tax should be paid by Lithuanian and foreign legal entities and organisations, as well as by Lithuanian and foreign individuals owning real estate in Lithuania. Lithuanian and foreign individuals owning real estate should pay the real estate tax if the real estate is used for their commercial activities (including the rent of real estate to legal entities).

The annual tax rate ranges from 0.3% to 1% of the taxable value of real estate.

Municipalities are entitled to establish a precise rate by 1 June of each year for the following year. The taxable value of the real estate is the average market value of the real estate established by applying the mass valuation method or the rebuilding value depending on the purpose of the real estate. However, the owners of real estate may request for individual valuation performed by independent property appraisers.

The annual tax declaration has to be filed with the tax authorities and the real estate tax has to be paid before 1 February of the following year. In addition, legal entities should pay advance real estate tax amounts equal to one-fourth of the annual tax.

Land tax is paid by the owners of private land and it amounts to 1.5% of the value of the land. Land tax does not apply to forest land, roads of common usage and land owned by embassies.

Land tax is paid annually for the whole calendar year if the land was acquired during the first half of the year. In the event that the land was acquired during the second half of the year, the first obligation to pay land tax arises the following year.

Legal and private persons leasing state or municipality owned land must pay a land lease tax, which is not less than 1.5% and not higher than 4% of the land value. A precise tariff for a land lease tax is established by the local municipality for each individual case. Land lease tax is paid according to the order established by the local municipality where the land is located. The land value on which the land lease tax is assessed is estimated according to special rules and is set forth in the land lease agreement.

## Other (*local taxes*)

Environmental taxes are applicable in Lithuania:

- pollution tax, which is paid by users of mobile (vehicles) and stationary (farms, factories) pollution sources for commercial purposes, and
- tax on environmentally harmful goods (accumulators, tyres, automotive filters, etc.) which is paid by the importers and Lithuanian producers of such goods, and
- packaging tax, which should be paid by the importers of packaged goods in to Lithuania or by Lithuanian manufacturers of packaged goods.

In general, these taxes are calculated (using special formulas) depending on the type of package/product/pollution source and the amount of pollution as well as specific consumer price index and of the level of achievement of any pollution avoidance target.

## Chapter 4

# Individual taxation

## Estonia

### Tax residency

An individual who has a permanent place of residence in Estonia or who stays in Estonia for at least 183 days over a period of 12 consecutive calendar months, or Estonian state public servants who are in the foreign service are considered resident for tax purposes.

### Personal income tax

#### Taxpayers

Resident taxpayers are subject to income tax on their world-wide income, non-residents are subject to income tax only on their Estonian source income.

#### Taxable income

Individuals are subject to general income tax at the rate of 21% on income derived in the calendar year from:

- employment (monetary payments)
- business (self-employed income)
- property/investment (rental income, interest on deposits and loans, royalties, capital gains on disposal of business, movable and immovable property)
- other sources (alimony and certain pensions, scholarships, grants, awards, lottery prizes, insurance indemnities and payments from pension funds).

Income tax at a rate of 10% must be withheld by a resident legal person on royalties, payments to artists and sportsmen/women for activities conducted in Estonia or on payments for services provided in Estonia when payments are made to non-residents.

Income tax rate of 10% is applied to amounts paid out under a contract of pension insurance with income tax incentives to a policyholder as well as to payments from pension funds to unit holders where:

- the policy or unit holder has turned 55 years of age but not before 5 years have passed since the entry into the contract or the initial acquisition of units
- the policy or unit holder has become permanently and completely unable to work
- after liquidation of the pension fund, or
- upon the death of the policy or unit holder, payments are made to the successor.

The annual taxable income of resident individuals is reduced by a basic personal allowance of EEK 27,000. An additional allowance up to EEK 27,000 is granted to a parent for each child aged 17 or less (in 2009 starting from the second child).

### Tax rates

Personal income tax is levied at a 21% flat rate.

### Tax exempt income

Tax-exempt income includes the following:

- dividends received from Estonian companies or if income tax has been paid on the share of profit or income tax has been withheld on the dividend in a foreign state
- capital gains from the sale of immovable assets, the essential part of which is a dwelling which was used by the taxpayer as his or her permanent or primary place of residence until transfer
- gains from the sale of movable assets for personal use
- certain child allowances and other social security subsidies
- state pensions up to EEK 36,000 in a calendar year
- certain scholarships and grants unless paid in connection with business or employment
- international and state cultural and scientific awards and sport awards complying with the conditions and order established by the government
- fringe benefits (tax is payable by employer)
- inheritance received (tax exempt is only the receipt of inheritance not sale henceforth)
- gifts and donations received from natural persons, a state or local government authority, a resident legal person or from a non-resident through or on account of its permanent establishment registered in Estonia

- indemnification paid to an employee for work accidents up to EEK 12,000 in a calendar year
- certain benefits received from insurance contracts
- pensions paid to policyholder on a regular basis after the policyholder has attained 55 years of age or after his or her total and permanent incapacity for work has been verified on the condition that the payments are made in equal or increasing amounts at least once every three months
- compensation for business trip expenses and daily allowances within the specified limits
- compensation for business use of a private car in accordance with certain regulations
- lottery prizes organised on the basis of an operating permit
- income derived from the first sale of land restituted in the course of the property reform
- interest paid by an EEA resident credit institution.

## Deductions

The following items are allowed as deductions for personal income tax purposes:

- alimony payments to resident natural persons (in certain cases non-residents as well)
- interest on housing loans and capital leases which is paid to the EU member state's resident banks
- training expenses (subject to conditions and limits set by the government)
- gifts and donations to specified persons and trade union entrance and membership fees up to certain limits (in total not more than 5% of the income of the period of taxation)
- contribution to certain pension funds with income tax relief (up to 15% of the income of the period of taxation).

The total amount of deductions may not exceed EEK 50,000 per taxpayer per year and not more than 50% of the taxpayer's taxable income.

## Foreign tax credit

A credit method is applied in order to avoid double taxation. Credit granted for foreign taxes paid is limited to the amount of Estonian tax payable on that income (ordinary credit) on a source-by-source basis. Taxpayers are required to submit a document certifying the payment of income tax. An exemption method is applied if the taxpayer

has received remuneration for working abroad and he/she has stayed in the foreign country for at least 183 days in any consecutive 12 month period and the remuneration was subject to taxation in this foreign country and the latter is certified.

### **Tax collection**

The period of taxation is a calendar year. The income tax return is filed with the tax authorities no later than 31 March of the following year. Income tax returns are prepared on a self-assessment basis and may be audited by the tax authorities for up to 3 years. Under certain cases, tax audits may occur up to 6 years after filing.

Married couples may file tax returns jointly (under certain conditions such as in the case of a non-resident husband/wife). Additional amounts of tax due must be paid to the Tax and Customs Board not later than by 1 July. Additional tax on business income or gains from transfer of property is payable by 1 October.

### **Social security tax**

Social security tax is paid by employers. Social tax at a rate of 33% is payable on wages and other monetary remuneration paid to employees. Tax is payable on a monthly basis.

Self-employed persons are liable to pay tax on their business income at a rate of 33%. During a calendar year advance payments of at least EEK 4,307 (in 2009) per quarter are made. The maximum social tax obligation for self employed is limited to the amount calculated from fifteen times minimum wage.

### **Unemployment insurance**

Unemployment insurance payments are shared between employer and employee. Employers pay tax at the rate of 0.3% on gross payroll payments and an additional 0.6% is withheld from payments made to employees. During 2009 the unemployment insurance contributions may be increased.

### **Pension insurance**

Funded pension payments are withheld at a rate of 2% from gross salary payments.

The payments of unemployment and pension insurance that are paid at the employee level are deductible from the taxable income. During 2009 changes may occur to the funded pension system.

## Capital taxes

There is no net wealth/capital tax in Estonia.

## Inheritance and gift tax

There is no inheritance or gift tax in Estonia, but if an individual sells inherited property and the gain from sale of such type of property is subject to income tax, the full sales price will be subject to income tax.

## Tax calculation example

The following example illustrates the calculation of taxes due on employment income paid to an Estonian resident.

1. Gross salary per month in EEK	10,000
2. Monthly non-taxable minimum	2,250
3. Unemployment insurance (0.6% of 1)	60
4. Pension insurance (2% of 1)	200
5. Monthly taxable income (1-2-3-4)	7,490
6. Personal income tax (21% of 5)	1,573
7. Net monthly income (1-6-3-4)	8,167

# Latvia

## Tax residency

An individual is a tax resident when:

- he/she has their permanent residence in Latvia
- he/she is present in Latvia for more than 183 days in a 12 month period
- he/she is a Latvian citizen and is employed overseas by the Latvian government.

There are no special procedures for terminating residence in Latvia. However, the Law on Taxes and Duties provides that an individual who will not be considered a tax resident in the following year, will no longer be a tax resident from the date they leave Latvia if they can show they have greater ties outside Latvia than within Latvia.

## Personal income tax

### Tax payers

Resident taxpayers are taxed on their worldwide income. Non-resident taxpayers are taxed on specific Latvian sources of income.

### Taxable income

Typical taxable cash and non-cash benefits of a compensation package are:

- salary
- reimbursements of foreign and/or home country taxes
- reimbursement of school tuition fees
- home leave reimbursements
- cost of living allowances
- expatriation premiums
- housing allowances/reimbursements
- company car
- medical insurance premiums paid by an employer
- incentive compensation.

Non-residents are liable for Latvian tax only in respect of Latvian source income including:

- employment income for duties performed within Latvia in favour of a Latvian or foreign employer, or performed outside Latvia for a Latvian employer
- income from independent professional services rendered to Latvian residents or registered permanent establishments within and outside Latvia
- income from professional services such as an artist, sportsman or trainer performed in Latvia
- income from performing duties as the member of a Board or supervisory body of a Latvian company



- income from a Latvian registered partnership
- income in the form of liquidation proceeds from the liquidation of a Latvian company that exceeds payable dividends
- income from the sale or use of immovable property located in Latvia
- income from the lease of movable property in Latvia
- income from agricultural production from "individual" farms
- dividends
- interest income, except interest from Latvian credit institutions
- income from intellectual property (royalties)
- insurance payments, if the agreement is concluded by an employer and it is terminated before a specified period
- pensions paid according to Latvian legislation.

### Tax rates

Latvian personal income tax is levied at a rate of 23%. Personal income tax rate for self-employed persons is 15%. An individual can choose to pay a fixed tax, if yearly income of his/her commercial activities does not exceed LVL 10,000. The tax year for individuals is the calendar year. Individuals are classified either as resident or non-resident taxpayers.

### Tax exempt income

Examples of some exempt income items are:

- dividends from Latvian companies and others registered in EU countries and EEA countries that have paid the full rate of tax on the profit from which the dividend is paid; otherwise a pro rata exemption is given
- income from deposits in Latvian EU and EEA registered credit institutions
- income from State bonds (Latvia , EU and EEA countries and Municipal securities)
- alimony payments
- some types of scholarships
- income from the sale of personal property; real estate must have been held for 12 months to be exempt.

The majority of exemptions do not apply to non-residents. However, if a resident of another EU or EEA country receives more than 75% of his annual income in Latvia, then the exemptions also apply.

## Deductions

There are limited deductions under Latvian Law. Deductible items are:

- mandatory social security contributions
- allowances for the support of close relatives or dependants (limited)
- donations to charitable organisations (limited)
- expenses related to the production of scientific, literary and artistic works (limited)
- contributions to private pension schemes (limited)
- non-resident taxpayers and individuals who are resident for less than six months in a tax year are only entitled to the standard deductions like social security contributions; special rules apply to the calculation of the income of a self-employed individual.

## Foreign tax credit

Where foreign taxes have been paid on income taxable in Latvia, a credit will be given. The credit is limited to the amount of Latvian tax that would otherwise have been payable on the amount. Proof that the tax has been paid is required.

Double Tax Treaty relief may also be available.

## Tax collection

Annual declarations must be filed by 1 April of the following year. Declarations are prepared on a self-assessment basis and may be audited up to 3 years after the tax became payable. If the tax liability assessed exceeds LVL 100, the tax can be paid over three months in equal instalments.

Personal income tax in respect of employment income is usually withheld from salary payments (payroll tax). All employers in Latvia, including foreign companies operating through a branch, must deduct payroll tax from remuneration paid to all employees and remit this tax to the tax authorities on a monthly basis on the salary payment date.

Foreigners working in Latvia for a non Latvian employer must register with the tax authorities and either the employer or the foreigner must, on a monthly basis, pay personal income tax based on their monthly salary.

## Social security tax

Mandatory social security contributions are payable in respect of gross employment income.

For individuals employed by a Latvian resident employer, the social security contribution rates in 2009 are:

Employer's rate – 24.09%

Employee's rate – 9%

If individuals are employed in Latvia by an employer which is resident in another EU or EEA member state, then contribution rates are the same as above.

If the employer is not resident in the EU or EEA, then the social contributions are:

- For Latvian citizens working in Latvia \* 33.09% (24.09%; 9%)
- For non Latvian citizens, who are in Latvia for more than 183 days – 31.13%

Foreigners who will be working in Latvia for less than 12 months can be exempt from Latvian social security contributions provided that social security contributions are paid in their country of residence.

There are some exemptions for EU and EEA citizens on short-term assignments.

## Unemployment insurance

Unemployment insurance payments are included in the monthly social security contributions.

## Capital taxes

There is no net wealth/capital tax in Latvia.

## Inheritance and gift tax

There are no inheritance or gift taxes in Latvia.

## Tax calculation example

Assume a married resident in Latvia with an employed spouse and one child, and a monthly income of LVL 180 as follows:

1. Gross salary in LVL	180.00
2. Less social security contribution (9%)	16.20
	163.80
3. Less monthly non-taxable income*	90
	73.80
4. Less allowance for dependent	63
5. Monthly taxable income (1-2-3-4)	10.80
6. Personal income tax (10.80 x 23%)	2.48
<b>Net monthly income (180-16.2-2.48)</b>	<b>161.32</b>

Social security contributions to be funded and paid by the employer are LVL 43: 24.09% of LVL 180 gross salary.

*\*Non taxable income is LVL 1,080 in a year or LVL 90 in a month*

## Lithuania

### Tax residency

Tax residency is determined by:

- permanent residence in Lithuania
- employment of a Lithuanian citizen abroad by the Lithuanian government
- foreign individuals staying in Lithuania for 183 days in a tax year or staying in Lithuania with or without breaks for 280 or more days during two consecutive tax years, whereby one stay in Lithuania during one of these years must be at least 90 days
- individuals whose place of personal, social and economic interest is Lithuania

### Personal income tax

#### Tax payers

Taxpayers are resident and non-resident individuals.

## Taxable income

Resident taxpayers are subject to income tax on their world-wide income, whilst non-residents are taxed on their Lithuanian source income only.

Taxable income of non-resident individuals includes the following:

- interest
- income from distributed profit
- income from the renting of immovable assets located in Lithuania
- authorship remuneration
- employment income (earned through a Lithuanian source including through a PE)
- income from sport activities
- income from performers' activities
- income from the sale of immovable assets located in Lithuania or movable assets which are registered in Lithuania.

## Tax rates

Personal income tax rates are 15% and 20%.

Twenty percent personal income tax applies to income from profit distributions (including dividends).

A fixed personal income tax prescribed by municipalities is imposed on income earned by individuals who have business activity certificates.

## Tax exempt income

Most important types of non-taxable income include the following:

- non-life insurance benefits and certain life insurance benefits
- certain types of pensions and annuities
- certain types of interest
- income from mariners from work on board vessels
- profit distribution from legal entities with unlimited liability which does not exceed LTL 4,000 (EUR 1,160) per taxable period
- income from agriculture if economic size does not exceed 14 European size unit
- income received by inheritance (subject to tax on inherited property)
- income received as a prize or by gift in certain situations

- certain capital gains
- certain scholarships
- pensions, rents, allowances, scholarships, premiums received from the state or municipality budget

Certain exemptions are denied in respect of items received from foreign entities registered or organized in a tax haven or individuals resident in a tax haven.

## Deductions

The following items are allowed as deductions for personal income tax purposes:

- life insurance premiums, subject to certain requirements
- pension contributions paid to the pension funds registered in Lithuania or another EU member state
- amounts paid by Lithuanian residents for higher education studies

## Foreign tax credit

Labour income earned and taxed in the EU-member countries or the countries with which Lithuania has a double tax treaty is treated as non-taxable income.

Other foreign income taxes that are substantially similar to Lithuanian personal income tax may be credited against the Lithuanian tax liability, limited to the amount of income tax actually paid in the foreign country. A proof, i.e. an official certificate issued abroad, proving that the tax has been paid indicating the amount thereof is required.

## Tax collection

The tax period is the calendar year. The annual tax return should be filed with the tax authorities by 1 May of the following year, with some exceptions.

Employers should withhold and pay personal income tax from labour remuneration and other similar payments made to employees..

## Social security tax

State social security contributions are mandatory for individuals working under employment contracts. Employees' contributions equal 3% of employment income and employers have to pay 30.98%. The employees' contributions must be withheld by employers.

Self-employed individuals are also liable to pay social security contributions.

EU Regulation (EEC) No. 1408/71, dated 14 June 1971, on the Application of Social Security Schemes to Employed Persons and their Families Moving within the Community and EU Regulation (EEC) No. 574/72, dated 21 March 1972, Fixing the Procedures for Implementing Regulation (EEC) No. 1408/71, have been implemented in Lithuania as of 1 May 2004. According to this legislation the individual will be subject to mandatory social security in the country where the work is performed, i.e. in the EU member state of the location of work functions. Therefore, foreigners fall under the requirement to pay social insurance contributions in Lithuania if their work functions are performed in Lithuania (except if an "E 101" form is obtained).

## **Health insurance contributions**

Starting from 1 January 2009, persons employed under a labour contract should pay 6% health insurance contributions. Permanent residents should also pay 6% health insurance contributions on other income which is subject to personal income tax. In accordance with the regulation, health insurance contributions should be paid on the dividends received, income from disposal of securities and real estate, income from individual activities, etc. The same rules apply for non-residents (except if an "E 101" form is obtained).

## **Unemployment insurance**

Generally, unemployment insurance provides benefits in case of termination of employment. Payers of unemployment insurance contributions should be insurers paying contributions for the individuals remunerated for the job performed. Unemployment insurance contributions should be calculated and paid together with all other social insurance contributions. Payments are equal to 0,1% of gross salary.

## **Capital taxes**

### **Real estate tax**

Individuals owning and using their real estate for commercial purposes are subject to real estate tax (see above).

### **Land tax**

Resident and non-resident individuals are subject to land tax collected by the municipal budgets at the rate of 1.5% of the taxable value. The assessment and payment terms are set forth by the municipalities, which are entitled to grant certain incentives.

## Inheritance tax

Taxpayers are individuals who received inherited property in Lithuania. Taxable property includes movable assets that have to be legally registered and immovable assets located in the Republic of Lithuania, shares and money.

Tax is not levied on the property inherited from close relatives or when the value of the inherited property does not exceed LTL 10,000 (EUR 2,900).

The rates of inheritance tax are as follows:

- 5% on inherited property, if the taxable value does not exceed LTL 0.5 million (EUR 144,800)
- 10% on inherited property, if the taxable value exceeds LTL 0.5 million (EUR 144,800).

## Tax calculation example

The following example illustrates the calculation of taxes on employment income (e.g. LTL 3,500) received by a married Lithuanian resident having one child:

1	Gross monthly salary (in LTL)	3,500
2	Main tax-exempt minimum <sup>1</sup>	0
3	One-half additional tax-exempt minimum for one child	50
4	15% income tax on LTL 3,450 (15% of 1-2-3)	517.5
5	6% health insurance contribution paid by the employee (6% of 1)	210
6	3% social insurance contribution paid by the employee (3% of 1)	105
7	Net salary (1-4-5-6)	2,667.5
8	30.98% social insurance contribution paid by the employer (30.98% of 1)	1,084.3
9	0.1% payment to Guarantee Fund (0.1% of 1)	3.5
10	Total employment cost for the employer (1+8+9)	4,587.8
11	Total tax burden for the employee (4+5+6)	832.5

Notes:

1. Main tax-exempt minimum is calculated based on the formula:  $470 - 0.2 * (\text{Gross monthly income} - 800)$ . Thus, if gross monthly income is over or equal to LTL 3,150 – no tax exempt minimum applies.



## Chapter 5

# Accounting and auditing

## Estonia

### Accounting

Since 1995, the Estonian accounting principles have been based on IFRSs. The current Accounting Act has been in force since 2003 with some minor amendments made during recent years to reflect the corresponding changes in IFRSs. According to the Act, commercial undertakings may choose whether to prepare their annual financial statements according to Estonian Accounting Standards (RTJ) or IFRSs. Listed companies, credit institutions and insurance companies are required to follow IFRSs.

The Estonian Accounting Standards are issued by the Accounting Standards Board which acts under the supervision of the Ministry of Finance. RTJs can be regarded as summarised and simplified versions of the corresponding IASs or IFRSs. When an RTJ does not cover a specific area, preparers of annual financial statements are encouraged to seek comprehensive or more detailed guidance from IFRSs. At the end of 2008, the Estonian Accounting Standards Board had issued 17 standards. The most important of them are:

RTJ 1	Underlying principles of annual financial statements
RTJ 2	Presentation of annual financial statements
RTJ 3	Financial instruments
RTJ 5	Tangible and intangible assets
RTJ 8	Provisions, contingent liabilities and contingent assets
RTJ 10	Revenue
RTJ 11	Business combinations and accounting for subsidiaries and associates

Most IFRS amendments effective from 1 January 2009 will also be reflected in the Estonian Accounting Standards.

As a general principle, RTJs require fewer disclosures than the corresponding IASs and IFRSs. The following are the most significant individual deviations from the principles of IFRS.

- Formats of the balance sheet and income statement and composition of different items are prescribed in the Accounting Act in more detail than in IFRS.
- Valuation of property, plant and equipment at fair value as a general principle is prohibited.
- Intangible assets can be valued only at amortised cost less impairment losses.
- Specific principles are determined for the accounting of business combinations between entities under common control.
- A number of areas such as accounting for joint ventures, employee benefits and accounting by retirement benefit plans and deferred income taxes are not covered by the RTJs as, in most of the cases, they are not significant in the Estonian business and legal environment.

As a general principle, groups of companies must prepare consolidated accounts. However, a number of exemptions are available. Groups are not required to prepare consolidated annual financial statements if at least two of the following three consolidated parameters are at the balance sheet date below the limits as defined in the Accounting Act: revenue EEK 10 million, total assets EEK 5 million and number of employees 10. Exemptions are also available for subgroups if the parent with more than 90% of voting power files consolidated annual financial statements either in Estonia or in another EU member state and in certain other less frequent cases.

From technical and administrative points of view, the following requirements of the Accounting Act should be emphasised:

- The Accounting Act sets a number of formal requirements to accounting source documents.
- Each entity has to prepare its internal regulations on accounting and the chart of accounts.
- Accounting registers can be maintained either as hard copies or in electronic form.
- As a general principle, accounting and related documents should be maintained for at least 7 years.
- Annual financial statements should be prepared in the Estonian language. However, the Act does not specifically limit the language in which every-day book-keeping should be arranged.
- An annual report includes the activity report and the declaration of management on their responsibility for giving the true and fair view of the financial position, result for the period and cash flows of the entity.
- Annual financial statements must be signed by all the members of the management board and supervisory board.
- Annual financial statements must be filed with the Company Registry within six months from the end of the financial year at the latest.

## Auditing

Audit has been compulsory for the majority of companies since 1991. The Authorised Public Accountants Act was adopted in 1999. This Act determines the requirements for auditors, the basis for passing the examination of professional competence, the legal basis for the professional activities of auditors and the organisation of the Institute of Auditors. In addition to the Act, the Estonian auditing rules have also been adopted. These include requirements for auditing and professional ethics based on the standards of the International Federation of Accountants. Under the rules, an auditor must provide auditing services in compliance with these rules and the standards of the International Federation of Accountants.

Under the Commercial Code, an audit is obligatory for all public limited companies. An audit is compulsory for private limited companies if their share capital exceeds EEK 400,000 or if the audit requirement has been established in the law or the Articles of Association of an entity.

In addition to the requirements of the Commercial Code, according to the Accounting Act auditing is compulsory for all entities meeting two of the following three criteria:

- net sales exceed EEK 10 million
- the number of employees exceeds 10
- total assets exceed EEK 5 million.

Auditors also perform other types of attestation engagements required by the Commercial Code, such as special reviews, merger and division reviews, and the providing of assurance on valuation of non-monetary contributions to share capital to mention some of the more significant examples.

According to the draft, the new Auditing Act that complies with the requirements of Directive 2006/43/EC of the European Parliament and of the Council should enter into force in Spring 2009. The new Auditing Act sets forth:

- 1) the legal basis for financial auditing;
- 2) the requirements for sworn auditors and audit firms;
- 3) the legal basis for the professional activities of sworn auditors and audit firms;
- 4) the requirements for public sector internal auditors;
- 5) the legal basis for the professional activities of public sector internal auditors;
- 6) the terms and conditions under which an audit or a review is mandatory and the basis for the activities of an audit committee;

- 7) the legal status and competence of the Board of Auditors and the basis for its activities, organization and financing;
- 8) the basis for the supervision of chartered internal and sworn auditors, audit firms and the Board of Auditors;
- 9) the basis for the maintenance of the register of auditors and audit firms.

Under the new Auditing Act, in performing their professional activities sworn auditors have to observe the international standards transposed by the European Commission and established by a Commission Regulation as well as the standards created in accordance with the principles and international standards developed by the International Federation of Accountants (IFAC). The professional activities of sworn auditors comprise audits, reviews, and verification of the legality of transactions.

In accordance with the new Act, an audit is mandatory for all state accounting entities, local governments and legal persons governed by public law. An audit is mandatory for an accounting entity within the meaning of the Accounting Act when at least two of the following reporting period figures in its annual financial statements exceed the following thresholds:

- 1) sales revenue or income: EEK 30 million;
- 2) assets as at the balance sheet date: EEK 15 million;
- 3) average number of employees: 30.

In addition, an audit is mandatory for an accounting entity within the meaning of the Accounting Act when one of the following reporting period figures in its annual financial statements exceeds the following thresholds:

- 1) sales revenue or income: EEK 90 million;
- 2) total assets as at the balance sheet date: EEK 45 million;
- 3) average number of employees: 90.

A review is mandatory for an accounting entity within the meaning of the Accounting Act when at least one of the following reporting period figures in its annual financial statements exceeds the following thresholds:

- 1) sales revenue or income: EEK 30 million;
- 2) total assets as at the balance sheet date: EEK 15 million;
- 3) average number of employees: 30.

# Latvia

## Accounting

Current Latvian accounting rules are based on the International Financial Reporting Standards adopted in the EU. The main objective of the Law of Accounting is to outline a system of accounting principles, and any other law or legislative act relating to accounting must be issued in conformity with this law.

Nine Latvian accounting standards are obligatory for financial statements:

- 1) guidelines on preparation of financial statements,
- 2) cash flow statement,
- 3) events after the balance sheet date,
- 4) changes in accounting policies, changes in accounting estimates and prior period errors,
- 5) construction contracts,
- 6) revenue,
- 7) fixed assets,
- 8) provisions, contingent liabilities and contingent assets,
- 9) investment property.

The following standards are at a draft stage: leases, income taxes and agriculture. Latvian Accounting Standards have only small differences from International Financial Reporting Standards.

The Law on Accounting applies to merchants, co-operative societies, foreign merchant branches and non-resident (foreign merchant) permanent representations, associations and foundations, political organisations (parties) and the associations thereof, religious organisations, trade unions, institutions, which are financed from the state budget or local government budgets, state or local government agencies, and to legal persons and natural persons who perform economic activities.

Accounting records must clearly display the transactions and the financial position of a company. The records must be kept in such a manner as to enable any person who is qualified in accounting to clearly identify the financial position of a company, as well as the business transactions performed in a given period of time, and to enable the person to ascertain both the beginning and the sequence of each transaction.

The company's general management has sole responsibility for any violation of the accounting regulations.

All company accounting records must be kept in Latvian currency. The company's books must be kept in Latvian language and, together with all the supporting documents, they must be kept within Latvia. If foreign persons participate in business transactions, another language may also be used. If codes, abbreviations, single letters or symbols are used in the records, explanations must be available.

A double entry bookkeeping system must be used, except for:

- individual merchants, individual undertakings, farms and fishing undertakings whose sales for the previous year do not exceed LVL 200,000, or other individuals who perform economic activities,
- religious organisations whose income from operating activities in the reporting year does not exceed LVL 25,000.

For establishments and organisations which are financed from the state budget or municipal budgets, required accounting records are prescribed by the Ministry of Finance.

Accounting records must be based on legally valid supporting documents, which contain the following information: the company's name, registration number, official address, document name, number, date, description and basis of transaction, indicators (amounts, volumes), parties involved (the persons directly entering into the transaction) and the signatures of persons responsible for the operating transactions and the correctness of information provided in the supporting documents. Some supporting documents may need additional information (stamp, seal, etc.), which are required by particular Cabinet Regulations.

All supporting documents, bookkeeping records, inventory lists, annual reports, as well as accounting policies and charts of accounts must be preserved in the company's archives for periods of 5 to 75 years. These include:

- ledger, annual reports and additions – 10 years (then transferable to public record office),
- inventory lists, accounting registers and accounting institutional forms – 10 years,
- source documents per calculated monthly salaries for staff – 75 years,
- other accounting source documents – 5 years.

If the company is under reorganisation or liquidation, it should prepare closing financial statements, if laws and regulations do not prescribe otherwise. Closing financial statements should be prepared, audited and published in accordance with laws and regulations applicable for annual reports.

## Annual report

The Annual Reports Law outlines the procedure for preparing annual reports and the presentation of financial statements. It applies to any commercial company, co-operative societies, individual undertaking, farm and fishing undertaking registered in Latvia, as well as to European economic interest groups and European commercial companies registered in Latvia. The law does not apply to those individual merchants, individual undertakings, farms and fishing undertakings whose revenue from business transactions in the prior financial year is less than LVL 45,000. This law does not apply to banks, savings and loan associations, commercial insurance companies in the form of joint stock companies, mutual insurance co-operative organisations, re-insurance, private pension funds, investment broker companies and investment administration companies. These prepare financial statements accordingly to IFRS as stated by the regulations of the Finance and Capital Market Commission.

Commercial companies which prepare financial statements in accordance with International Financial Reporting Standards as adopted by the European Union in accordance with the Finance and Capital market Commission requirements may derogate from the requirements of the Annual Reports Law.

The reporting year should comprise of 12 months and usually corresponds with the calendar year. A company may have another start and end of the reporting year if required by the company's Articles of Association. The initial reporting year of a newly established company may comprise a shorter or longer period of time, but no more than 18 months. If the starting date of an already existing company is changed, the reporting year may not be longer than 12 months. The fiscal year should be similar for the parent company and subsidiary companies, which are merged into one concern (group).

The annual report must be completed for each year, and it consists of:

- the financial statements.
- the management report on the development of the company in the current year.

The financial statements contain the balance sheet, the profit and loss statement, cash flow statement, statement on changes in shareholders' equity and notes to the financial statements.

Not later than one month after the approval of the annual report by a shareholders' meeting and, at the latest, four months after the end of the fiscal year, the audited annual report must be filed with the tax authorities. The tax authorities submit an electronic version of the annual report to the Enterprise Register within five working days. The Enterprise Register publishes an announcement in the national publication *Latvijas Vestnesis* that the information is publicly available in the Enterprise Register.

The date of submission of the annual report is extended to seven months after the end of the fiscal year for companies with:

- assets of LVL1,000,000 or greater,
- sales of LVL2,400,000 or greater, and
- an average number of employees during the fiscal year of at least 250.

All annual reports submitted to the tax authorities of the Republic of Latvia are stored in the files of the respective registered enterprises, and are publicly available from the Enterprise Register.

All items in the annual report shall be in accordance with the following policies:

- Assumption that the company will continue as a going concern;
- Consistent valuation principles with those used in the prior year;
- Items are valued conservatively i.e.:
  - Annual report reflects only the profit generated to the date of the balance sheet;
  - All incurred liabilities and current or prior year losses have been taken into consideration even if discovered within the period after the date of the balance sheet and preparation of the annual report;
  - All impairments and depreciation have been taken into consideration irrespective of whether the financial result was a loss or profit.
- Income and expenses incurred during the reporting year have been taken into consideration irrespective of the payment date or date when the invoice was issued or received; expenses are matched with revenue within the proper reporting period;
- Asset and liability items have been valued separately;
- The opening balance sheet agrees with the prior year closing balance sheet;
- All material items, which would influence the decision making process of users of the annual report have been recognised and insignificant items have been combined and their details disclosed in the notes;
- Business transactions are recorded taking into account their economic contents and substance, not the legal form.

The reporting conditions may be disregarded in exceptional cases, but such action must be recorded and justified in the notes, indicating its effect on the assets, liabilities and financial results of a company.

Financial instruments may be measured at fair value in accordance with IFRS.

The law provides four options of presentation of the profit and loss account from which the enterprise must choose. Two options classify expenses by periods and two options by turnover. The presentation should not be changed unless there are good reasons.



The notes to the financial statements should explain the valuation methods used and substantiate any changes in valuation policies. They should also disclose information concerning the substance of specific items, e.g. sales by region and field of activity, taxes paid during the year and tax deductions and benefits received, as well as the total number of persons employed.

A management report should contain clear information on the company's development and current financial position, as well as information on significant risks and unclear circumstances met by the company during the reporting period. A management report also should include information on the impact of environmental protection requirements, if material, as well as on financial instruments and financial risk management policies. Significant non-financial indicators should also be disclosed. The management report should describe subsequent events significantly affecting the financial position. A vital part of the management report is the proposed distribution of profit or loss coverage plans.

### Consolidated annual reports

On 1 January 2000, the Consolidated Annual Reports Law came into effect. This Law states the general regulations for the preparation of consolidated annual reports as well as the exceptions from the requirement to prepare a consolidated annual report. A participant registered in Latvia is exempt from the obligation to prepare consolidated annual reports for its group of companies if it, together with its subsidiary companies, does not exceed at least two of the following criteria for two consecutive years:

- assets of LVL 1,000,000,
- sales of LVL 2,400,000,
- an average number of employees during the fiscal year of 250.

A Parent company registered in Latvia, which is at the same time a subsidiary company of another group of companies, is exempt from the obligation to prepare consolidated annual accounts if its parent company is a company registered in Latvia or in another Member State of the EU which is in compliance with at least one of the following conditions:

- it owns all (100%) of the stock or shares in the company which is exempted from the obligation to prepare consolidated annual accounts or
- it owns at least 90% of the stock or shares in a company which is exempt from the obligation to prepare consolidated annual accounts, and the remaining stockholders or shareholders (minority stockholders) of this company have agreed (are informed and do not oppose) to the application of the exemption.

The Consolidated Annual Reports Law also states the procedures for the preparation, examination, approval and publication of consolidated annual reports. A parent company may prepare consolidated financial statements in accordance with IFRS.

The Law on Concerns (groups) took effect on 27 April 2000. Dependant companies should prepare a dependency statement, if a concern contract has not been concluded. The dependency statement provides a general overview on the relationship between the dependant company and the dominant entity. The dependency statement should be approved together with the annual report. The dependency statement is subject to review by a sworn auditor together with the annual report of the dependent company.

## **Auditing**

Financial statements are subject to an audit by a Latvian sworn auditor if the company exceeds two of the following listed criteria:

- assets of LVL 250,000,
- sales of LVL 500,000,
- 25 employees during the fiscal year.

These criteria relate to financial periods starting on 1 January 2007 or later.

Effective 1 January 2002, the Law on Sworn Auditors was enacted, which provides that the audit must be conducted in accordance with the International Standards on Auditing recognised in the Republic of Latvia. Sworn auditors' commercial companies are licensed in accordance with the law On Sworn Auditors.

# Lithuania

## **Accounting**

Key requirements for accounting are provided by the Law on Accounting.

Commercial undertakings must perform accounting and prepare financial statements in accordance with Lithuanian Business Accounting Standards (LBAS). Entities may choose IFRS as their accounting and reporting framework. Once the choice is made it cannot be changed within 5 years, except a case when the entity is becoming a member of a Group of entities.

Undertakings, whose securities are traded in the regulated markets, must follow IFRS as adopted by the EU when preparing financial statements.

Lithuanian Business Accounting Standards are issued by the Institute of Accounting which acts under the supervision of the Ministry of Finance. LBASs can be regarded as summarised and simplified translations of the corresponding IASs or IFRSs at the date of their adoption.

At the end of 2007 there were 33 LBASs approved by the Institute.

As a general principle, LBASs require less disclosure than the corresponding IASs and IFRSs. However, LBASs do follow the benchmark treatments of IASs at the date of their adoption and do not provide for alternatives.

Groups of companies are required to prepare consolidated accounts. A parent company, which is a subsidiary of an ultimate parent company registered in Lithuania and preparing a consolidated financial statement, need not prepare consolidated financial statements if one of the following conditions is present:

- all shares of the company are owned by the ultimate parent
- not less than 90% of the shares of the company are owned by the ultimate parent and minority shareholders do not claim against non preparation of the consolidated financial statements.

In addition, the parent company is not obliged to prepare consolidated financial statements unless at least 2 of the following ratios for the group are exceeded:

- net turnover (before inter-company eliminations) – LTL 30,000,000
- total assets (before inter-company eliminations) – LTL 18,000,000
- average number of employees – 75.

From the technical and administrative points of view, the following requirements of the Law on Accounting should be outlined.

- Accounting in a company can be performed by an internal accounting department (chief accountant) or by a third-party company providing accounting services.
- The Law sets a number of formal requirements for accounting source documents.
- Each entity has to prepare its accounting policies and the chart of accounts, which must be approved by the general manager.
- Accounting registers can be maintained either as hard copies or in electronic form, but print outs are still required.
- Accounting must be made in LTL, or if necessary may be made both in LTL and foreign currency.

- Accounting must be conducted in the Lithuanian language, or if necessary may be both in Lithuanian and a foreign language.
- The general manager is responsible for the organising of accounting and storing of accounting documents.

Legal requirements for financial statements are set in the Law on Financial Statements and the Law on Consolidated Financial Statements. Certain reporting requirements are set in the Company Law.

- Financial statements are signed by the general manager of the company and must be approved following procedures set in the by-laws of the company.
- Consolidated financial statements are signed by the general manager of the parent company and must be approved following procedures set in the by-laws of the company.
- Before the general shareholders' meeting, the board (managing director) must prepare an annual report on the company's activities.
- Companies must submit their annual financial statements for shareholder's approval within four months after the end of a financial year.
- Companies must present annual financial statements (consolidated financial statements) to the company register within 30 days of approval by the general meeting.

## Auditing

The Law on Audit provides regulations on auditing activities. The law determines the requirements for auditors, the basis for passing the examination of professional competence, types and requirements for audit companies and the organisation of the auditor's chamber. The Law on Audit provides the rights, duties and responsibilities of the auditors and audit companies. Following the law, audit shall be performed in accordance with National Auditing Standards or International Standards on Auditing as promulgated by the International Federation of Accountants.

Following the Company Law, the shareholders meeting is authorised to appoint or remove an auditor for the company. The annual financial statements of private or public limited liability companies are subject to a statutory audit, if a company meets two of the following criteria:

- annual turnover exceeds LTL 12,000,000
- total assets exceed LTL 6,000,000
- average number of employees exceeds 50.

Besides auditing, an auditor must review the annual report on the company's activities.

## Chapter 6

# Employment

## Estonia

At the end of last year the Estonian Parliament passed a new Employment Contracts Act which will be in force from 1 July 2009.

The new Act integrates all of the legal provisions regulating labour relations that used to be set out in a number of different acts (Wages Act, Holidays Act, Working and Rest Time Act and Labour Code).

The Act was drafted taking into account the EU labour law directives, the obligations under the European Social Charter that are obligatory for Estonia, and the conventions and the recommendations of the International Labour Organisation that have been ratified by Estonia.

### Employment contracts

In the new Employment Contracts Act, an employee is not treated as the weaker party in an employment relationship. The employment contract is just another contract under the law of obligations. The principle of freedom of contract is applied under which the parties to an employment contract are free to shape the content of the contract. The previous Act imperatively prescribed most of the contract terms. According to the Estonian labour law, an employment contract is an agreement between an employee and an employer under which the employee undertakes to do work for the employer in subordination to the management and under the supervision of the employer, and the employer undertakes to provide the remuneration and the working conditions provided for in the agreement between the parties, a collective agreement, law or administrative legislation.

Employment contracts in Estonia may be entered into for an unspecified term or a specified term of up to 5 years. Employment contracts may be concluded for a specified term only in certain cases, for example for the replacement of an employee who is temporarily absent or for the performance of temporary work, primarily in the event of a temporary increase in work volume or seasonal work.

Employment contracts must be in written form unless in effect for a period not exceeding two weeks. Employment contracts may prescribe a probation period of no more than four months.

Parties may specify in the employment contract mutual relations, which are not regulated by the labour law, matters concerning business secrets and competition. In that case their relations will be regulated by both the labour law and the law of obligations.

## Remuneration

Since January 2008 the monthly minimum wage for full-time work has been EEK 4,350. Overtime work may be compensated by time off or additional remuneration depending on the agreement of the parties. Additional overtime pay per hour has to be at least 50% of the employee's average hourly wage.

Work performed on a public holiday is remunerated at least at double the normal rate, regardless of whether such work is scheduled or unscheduled. At the request of an employee, an employer may compensate for unscheduled work performed on a public holiday with time off in lieu of money, to the extent of the time worked. In such cases, work performed on a public holiday is remunerated as work performed on an ordinary working day.

Work performed in the night (from 10pm to 6am) should be additionally compensated for at the rate of 25% of the hourly wage rate of the employee, unless it has been agreed in the employment contract that the basic salary includes the additional remuneration.

Wages must be paid at least once a month.

## Working time

A typical working week consists of five working days from Monday to Friday (full work time). The general national standard for the working time of employees is eight hours per day or 40 hours per week; the duration of one shift may not exceed 12 hours. Working time may be calculated also by using the recording of total working time.

Overtime is allowed by mutual agreement. Working time together with overtime may not exceed an average of 48 hours per week during a four-month recording period. The absolute limit for working time and overtime is 52 hours per week during a four-month period, if the employee agrees to do overtime and overtime work is not unreasonably harmful.

The duration of annual paid vacation is 28 calendar days. Vacations exceeding 28 days are made available to employees in specific fields.

By agreement of the parties, annual leave may be granted in parts. However, the duration of one continuous period of leave must be at least 14 calendar days.

Employees may be granted a leave without pay at their request for a period of time established by agreement of the parties. The law prescribes some occasions when the employee is entitled to unpaid leave.

A woman is entitled to a pregnancy and maternity leave of 140 calendar days. A woman has the right to commence pregnancy and maternity leave at least 70 calendar days before the estimated date of delivery.

A mother or father of a child may be granted child-care leave at his or her request for raising a child of up to 3 years of age.

A father has the right to additional child-care leave of 10 working days that may be taken during the two months preceding the expected date of childbirth or during the two months following the birth of the child.

A mother or a father is also entitled to additional child-care leave of three to six calendar days every working year depending on the number of children and their age.

Employers do not have the right to withhold vacation and employees do not have the right to waive vacation. The employee's claim for vacation is valid for the vacation available for one preceding year.

## **Termination of employment**

An employee may terminate an employment contract with an unspecified term by giving the employer 30 calendar days' notice. Employers and employees should inform each other of any intention to terminate the employment contract. It is possible to terminate the contract by mutual consent at any time.

An employer has a right to terminate the employment contract only on the grounds specified by law. The employer is obliged to justify the need to terminate the employment contract to the employee. Depending on the basis for termination and how long the employee has been continuously employed by the employer, an employer is obliged to give the employee 15 to 90 calendar days' notice.

An employer is responsible for paying the final severance pay on the day of termination.

If an employment contract is terminated because of redundancy, the employee is entitled to unemployment insurance benefits on the basis of and pursuant to the procedure established in the Unemployment Insurance Act.

## **Expatriates and immigration law**

Immigration legislation in Estonia is governed principally by the Aliens Act (effective from 12 July 1993 and amended many times) and the Citizen of the European Union Act (effective from 1 August 2006)

A residence permit may be temporary (validity period up to five years) or long-term.

A temporary residence permit may be issued to a foreigner:

- married to a person with a permanent residence in Estonia;
- for settling down with a close relative permanently residing in Estonia;
- for working;
- for studies at an Estonian educational institution;
- for business;
- whose permanent legal income ensures his/ her subsistence in Estonia;
- whose application for residence permit is based on an international agreement.

A temporary residence permit may be extended if the basis for the permit has not changed and the application is justified. A foreigner residing in Estonia on the basis of a temporary residence permit who desires to stay outside Estonia for more than 183 days per year has to register his/ her absence from Estonia with the Citizenship and Migration Board.

A long-term residence permit may be issued to a foreigner who has stayed in Estonia permanently on the basis of a temporary residence permit for at least five years, holds a valid temporary residence permit, has a registered residence, health insurance and permanent legal income for subsistence in Estonia and has knowledge of the Estonian language at least at a basic level.

In order to work in Estonia, a citizen of a foreign state needs to obtain a permanent residence permit or, in addition to a temporary residence permit, a work permit.

The following persons do not require a work permit in order to work in Estonia:

- foreigners with long-term residence permits;
- foreigners who have residence permits for employment;
- foreigners who have applied for a residence permit before 12 July 1995 and who have obtained such a permit;
- imprisoned persons during their stay in prison;
- members of locomotive crews;
- staff serving in locomotives and trains;
- drivers for taking passengers or cargo over state borders;
- foreigners who hold a residence permit for settling with a close relative who is residing – permanently in Estonia;



- foreigners who hold a residence permit for settling with a spouse;
- foreigners who hold a residence permit issued on the basis of an international agreement.

For short-term employment not exceeding a period of six months during a year, a work permit is not required. This will apply to foreigners who stay in Estonia either on the basis of a visa or on a visa-free basis.

A foreigner's activities as a sole proprietor and his/her work under an employment contract, service contract or another contract is deemed to be employment in Estonia.

A citizen of the European Union may freely stay and work in Estonia for the first three months. To work for a longer period, a right of residence must be registered. A working permit is not necessary. A citizen of the European Union acquires temporary right of residence in Estonia for 5 years if such a citizen registers his or her residence according to the procedure provided in the Population Register Act.

Estonia joined the Schengen area on 21 December 2007.

## Trade unions

According to the Estonian Trade Unions Act employees have the right to be members of trade unions of their workplace or other trade unions. A trade union may be founded by at least five employees, while a federation of trade unions may be founded by at least five trade unions.

Trade unions have the right to represent their members in collective labour relations and in personal labour relations on the basis of authorisation from their members. Unions may, for example, conclude collective agreements with employers, represent their members in labour dispute resolution bodies, etc.

The majority of employees belonging to trade unions are employed in the public sector. Only 10% of employees in Estonia belong to trade unions.

# Latvia

## Employment contracts

An employment contract must be concluded for an indefinite period of time, except if it is in order for the employee to perform specified short-term work only in cases specified by the Labour Law. The period of the employment contract concluded for a limited period of time cannot be more than 3 years (including any extensions of the term).

The Labour Law balances employers and employees rights in accordance with EU directives, International Labour Organisation treaties and requirements of the European Social Charter.

Employees and employers can agree upon the law to be applied to employment relations. If an employee and employer do not choose an applicable law, the laws of Latvia or a state where the employee performs his work, or the laws of the country of the place of location of the employer, or the laws of the country to which legal labour relations are closely connected, will apply.

When concluding an employment contract, a trial period of a maximum of three months may be established for the purpose of determining whether an employee is capable of the performance of work entrusted.

The employee is obliged not to divulge information which is a commercial secret of the employer. Agreements between employee and employer on the limitation of professional activity after the termination of legal employment relations are permissible in certain cases.

## **Remuneration**

Minimum wage is LVL 180 starting from 2009. Employees who perform overtime work must be paid double for these additional hours.

Wages must be paid twice a month, unless employer and employee have agreed that the wage will be paid only monthly.

## **Working time**

Regular daily work time cannot exceed eight hours and the regular weekly work period is 40 hours. Overtime is permissible if the employer and the employee have agreed upon it in writing. Overtime work cannot exceed 144 hours during a four-month period.

Each employee is entitled to a paid annual vacation. Such vacation, excluding public holidays, cannot be less than four calendar weeks. By agreement of the parties, annual leave may be granted in portions, but the duration of one continuous period of leave must be at least 14 calendar days. In exceptional cases vacation can be transferred to the next year; however, in this case, vacation during the current year cannot be shorter than two consecutive weeks. The part of the vacation transferred to the next year should be combined with the next year's vacation when possible. Current year vacation may be postponed for one year only.

Women are entitled to pregnancy and maternity leave of 112 calendar days. These days are not included in the annual vacation. Paternity leave may be granted to a father for a period of 10 days. Such leave must be granted not later than two months after the birth of a child.

## Termination of employment

The employee has the right, a month in advance, to give notice to the employer regarding termination of an employment contract in writing, unless a shorter period for giving notice is established in the employment contract or in a collective agreement. An employment contract can be terminated by mutual agreement of the employer and employee at any time.

An employer has a right to terminate the employment contract only on grounds specified by law. The employer is obliged to justify the need to terminate the employment contract in writing to the employee.

An employer is responsible for paying the final severance pay on the day of termination.

If an employer foresees collective termination of employment agreements with employees, the employer must give notice to the State Employment Agency at least 60 days' prior to the collective termination of employment contracts.

## Expatriates and immigration law

The Immigration law has been amended several times to be in line with the EU law, especially by the transposition of directives regarding the free movement of persons within the EU. For citizens of countries other than EU member states, visas or residence permits are required. There is a special procedure to receive visas which varies depending on the circumstances of each individual case. There are numerous nationalities which do not require visas to visit Latvia for a short time.

Persons who are non-EU citizens must obtain work and residence permits in order to work in Latvia. A permit is issued for a particular job with a particular employer and may be for a limited period, which can be extended. The specifics of the work permit application process differ depending on the occupation.

EU citizens do not have to obtain a work permit in order to work in Latvia. An expatriate who is an EU citizen must register at the relevant authority to receive a registration certificate if he/she plans to reside in Latvia for more than 90 days within a 6 month period. EU citizens have the right to apply for the registration certificate if certain criteria are met, if one of the criteria is work. Family members of the EU citizen enjoy residence rights along with the EU citizen, as provided in EU law.

## Trade unions

The Latvian Trade Union Law states that a trade union can be formed if it consists of at least 50 members or at least 25% of employees working for a particular enterprise, profession or industry.

Trade unions have the right to represent their members in collective labour relations and in personal labour relations on the basis of authorisations from the members. Unions may, for example, conclude collective agreements with employers, represent their members in state institutions and in courts.

## Lithuania

### Employment contracts

The main legal act regulating labour relations in Lithuania is the Labour Code. The Labour Code sets the terms and conditions of employment contracts, working and rest time, remuneration, liability, etc. Parties to an employment contract may also agree on other terms, i.e. a probation period of up to three months, confidentiality obligations, etc. However, as a general principle, an employment contract may not accord an employee terms and conditions that are less favourable than those established by law.

Specific labour areas, such as activities of work councils, trade unions, and participation rights of the employee are regulated by separate special laws.

An employment contract must provide the following substantive terms of employment: place of work, work duties and/or position and remuneration. The substantive terms of an employment contract can be changed only after obtaining an advance written consent by the employee. An employment contract must be concluded in writing according to the model form employment contract approved by the law.

The Lithuanian Labour Code provides for the following types of employment contracts:

- employment contract concluded for an indefinite period of time
- fixed-term, temporary and seasonal employment contract
- employment contract for additional work and secondary work
- employment contract with home-workers
- employment contract on the supply of services.

Generally, employment contracts are concluded for an indefinite period of time.

A fixed-term employment contract may be concluded for a certain period of time or for the period of performance of certain work, but cannot exceed a 5-year term. A fixed-term employment contract cannot be concluded for work which is deemed as permanent.

A seasonal employment contract may be concluded for the performance of seasonal work, which due to natural and climatic conditions may not be performed all year round, but in certain periods (seasons), not exceeding eight months (in a period of 12

successive months), and which is included in the list of seasonal work approved by the Lithuanian Government.

A temporary employment contract shall be an employment contract is concluded for a period not exceeding two months.

An employee may agree on an arrangement to perform certain additional duties or certain additional work (not agreed in the main contract) at the same workplace and conclude an employment agreement on additional work.

An employment contract with home workers must establish that an employee will perform job functions at home. A contract on the supply of services is an employment contract whereby an employee undertakes to supply personal household services to his employer.

Employment contracts as well as amendments thereof must be in writing and registered in the internal register of employment contracts of a company.

## Remuneration

Remuneration to be agreed in the employment contract must not be less than the minimum monthly salary established by the Government (i.e. LTL 800 - approximately EUR 232 – as of 1 January 2008).

Overtime work or night work (from 10pm to 6am) must be paid by at 1.5 times the usual rate.

Unscheduled work during rest days or public holidays must be paid at double rate or upon the employee's request an additional rest day may be granted.

## Working time

Normal working hours are 40 hours per week. Generally, working hours including overtime may not exceed 48 hours during a 7-day period. Overtime may not exceed four hours within two days and 120 hours per year. The collective agreement may indicate other terms of overtime, however, even then the total overtime may not exceed 180 hours per year.

An employee is entitled to 28 calendar days of annual paid vacation after he/she has worked at a company for six months. Annually, 35 days of paid vacation must be granted to certain categories of employees as follows:

- employees under 18 years of age
- employees who, as single parents, are raising a child younger than the age of 14, or a disabled child younger than the age of 18
- disabled persons.

Extended annual leave up to 58 calendar days must be granted to certain categories of employees whose work involves greater nervous, emotional and intellectual strain and professional risk, as well as to those employees who work in special working conditions.

Employees having more than a 10-year work record in a company are entitled to an additional three annual paid vacation days.

## Termination of employment

An employment contract may only be terminated on the grounds explicitly provided by legislation and in accordance with the statutory termination procedures. The termination grounds include mutual agreement, the employee's request, the employer's initiative, etc.

The requirement to pay final severance pay as well as the compensation amount depends on the particular reason for the termination. If the employment contract is terminated due to the employee's fault, no compensation is to be paid. If the employee is not at fault, severance pay may vary from one to six average monthly salaries depending on the work record of the employee. The legislation also provides for some additional requirements, such as advance notice of two months (in certain cases four months), priority to stay at work, etc., which must be adhered to when terminating an employment contract.

It is prohibited to terminate an employment contract with a pregnant woman or with an employee having a child under three years of age, unless the employee is at fault. Employment may not be terminated when the employee is ill or during vacation time.

## Expatriates

Expatriates may work in Lithuania under an employment contract provided they have obtained work permits. However, work permits are not required for citizens of the EU-member states.

There is also a group of citizens of non-EU states who are relieved from the obligation to obtain work permits. The exemption applies to:

- managing directors of Lithuanian companies registered with the Company Register
- persons registering a company in Lithuania and owning at least 10% of shares thereof
- persons coming to Lithuania to take care of negotiations regarding conclusion and implementation of agreements, staff training, commercial establishment for a period not longer than three months per year
- persons who are citizens of non-EU countries but are working in the EU and have the social insurance for temporary work in Lithuania (form E 101), etc.

Work permits are issued by the State Labour Exchange. The whole procedure of issuing a work permit for an employee who will be employed by a Lithuanian company takes two months after the relevant documents have been submitted to the State Labour Exchange. A work permit for a person working in Lithuania on a business trip must be issued within one month after the relevant documents are submitted to the State Labour Exchange.

Citizens of non-EU states must also have a temporary residence permit to stay in Lithuania for the purposes of work. Residence permits are issued by the Immigration Department at the Ministry of Internal Affairs. The procedure for issuing a temporary residence permit takes 4-6 months. The temporary residence permit may be issued for a maximum of five years.

Citizens of the EU-member states are not required to obtain the residency permits in Lithuania. However, the EU-member state citizens intending to stay in Lithuania for a period exceeding three months within half-year from their first day of entry to Lithuania must declare their residence place in Lithuania. Non-EU citizens who are the family members of the EU citizens intending to stay in Lithuania for a period exceeding three months in any calendar half-year must obtain an EU residency permit. This permit is issued by the Immigration Department at the Ministry of Internal Affairs. The procedure of issuing the EU residency permit takes one month.

EU-member state citizens legally residing in Lithuania for the previous five years may acquire the right to permanent residency in Lithuania.

An employment contract with a foreigner who is not exempted from obtaining a work permit must be concluded in accordance with the standard form of the employment contract. It is forbidden for the employee to engage in the work other than that specified in the work permit. The employment contract with a foreigner who is not exempted from obtaining a work permit must be registered with the National Labour Exchange within three days from its signing.

## **Immigration law**

Any non-EU citizen arriving and staying in Lithuania is subject to the regulations set by the Council (EC) Regulation No. 539/2001 listing those countries whose nationals must be in possession of visas when crossing the external borders and those whose nationals are exempt from that requirement.

Any foreigner who is subject to a visa free regime is eligible to stay in Lithuania without visa for three months within half a year from their first day of entry into Lithuania or any other Schengen state.

Any foreigner having a valid Schengen visa is entitled to enter Lithuania and stay for the period permitted by the visa; however not longer than three months within a six month period.

A family member of an EU citizen who is not an EU citizen, but holds a residence permit prescribed by the Directive 2004/38/EC of the European Parliament and of the Council of 29 April 2004 on the right of citizens of the EU and their family members to move and reside freely within the territory of the member states, is allowed to stay in Lithuania three months within a six month period.

There are two types of visas: Schengen visa and national visa.

Schengen visa types include:

- airport transit visa (A);
- transit visa (B);
- short-stay visa (C).

Visas might be single-entry, dual-entry or multiple-entry visas.

A national visa for a single entry (D) may be issued to a foreigner who has been granted a permit of temporary or permanent permit to live in Lithuania.

A national visa for multiple entries (D) may be issued if a foreigner submits the documents proving that he/she intends to enter Lithuania periodically, while his/her main place of residence is in a foreign state and there is no requirement for the foreigner to get a temporary residence permit in Lithuania.

Visas are issued at diplomatic missions or consular offices of the Republic of Lithuania abroad.

## **Trade unions**

Trade unions may be established on the basis of professional, territorial and other principles.

Persons legally working in Lithuania may be members of trade unions. Trade unions can be founded based on territorial, professional or any other ground.

There must be at least 30 founders of a trade union or the number of the founders may not be less than one-fifth (at least three employees) of all the employees in a company. Trade unions must be registered with the Register of Legal Persons within six months after the statutory foundation documents have been adopted.

Trade unions have the right to negotiate collective agreements. They may also organise strikes and participate in solving individual and collective labour disputes.



## Chapter 7

# Real estate

## Estonia

### Registration

All immovables and rights relating to immovables in Estonia are entered into the public Land Register, maintained by the land registry departments of the county courts. Ownership and other rights relating to immovables are created upon entry into the Land Register. The current Estonian model is based on the private law transparency principle, following the example of the respective continental-European civil law tradition.

### Movable and immovable property

Immovables are plots of land together with their essential parts – things permanently attached to the plot of land (e.g. buildings, forest, etc.) and the rights relating to the plot of land.

The general principle provides that all things that are not immovables, i.e. not to be entered into the Land Register, are movables. In separate cases, buildings may also be treated as movables if they are not parts of an immovable, such as unfinished buildings constructed on a legal basis, or apartments which are not registered as apartment ownerships.

### Acquisition

Foreigners are allowed to acquire immovables in Estonia with certain conditions and restrictions provided by the Restrictions on Acquisition of Immovables Act. There are two main types of restrictions on the acquisition of immovables:

- restrictions arising from public interest on the acquisition of 10 hectares or more of agricultural or forest land
- restrictions arising from national defence reasons on the acquisition of land in certain regions of Estonia.

Without conditions, 10 hectares or more of agricultural or forest land may be acquired by Estonian citizens. Citizens of states party to the EEA Agreement and legal entities can also acquire such land, provided that the following conditions have been met.

- Citizens of states party to the EEA Agreement (hereinafter Contracting States):
  - permanent residence in Estonia for at least the last 3 years before the acquisition
  - engagement in agricultural production or forest management as sole proprietors in Estonia for at least 3 financial years.
- Legal entities entered into the Estonian commercial register or legal entities of Contracting States, who have a branch in Estonia:
  - production of agricultural produce or forest management must be included as an area of activity in the articles of association (forest land may also be acquired by legal persons whose activity is the production of agricultural produce)
  - engagement in the respective area of activity in Estonia for at least 3 financial years.

Without meeting the above requirements, 10 hectares or more of agricultural or forest land can only be acquired with the authorisation of the county governor. The restrictions listed above will not apply in their present form after the end of the transition period concerning the acquisition of agricultural and forest land provided for in the agreement of Estonia's accession to the European Union.

Restrictions exist for national defence reasons to prohibit persons who are not citizens or legal entities of Estonia or of Contracting States from acquiring immovables on certain sea islands, border cities and rural municipalities listed in the Restrictions on Acquisition of Immovables Act. The Government may grant authorisation for the acquisition of an immovable in the above also to other persons for reasons significant to the State.

Aside from transfer of real rights to an immovable, rights of use may be granted with lease or commercial lease contracts, primarily regulated by the Law of Obligations Act. There is no requirement to notarise such contracts and a corresponding notation in the Land Register is optional.

## **Real estate contracts**

Rights relating to immovables in Estonia are regulated by the Law of Property Act, entered into force on 1 December 1993. The rights, i.e. certain rights belonging to a person regarding a movable or immovable object, are ownership (right of ownership) and restricted rights, such as servitudes, encumbrances, right of superficies (building title), right of pre-emption and right of security. The transfer of immovable property ownership or its encumbrance with a right must be concluded with a notarised transfer contract, which would lead to a corresponding entry in the Land Register.

As one of such rights, an immovable may be encumbered with a right of superficies (i.e. building title), leading to the creation of an independent Land Register part with a transferable and inheritable right to temporarily own a construction on the immovable of another. Only one right of superficies may be established on an immovable, for a specified term not longer than 99 years.

## **Mortgage**

As an instrument to facilitate credit, immovables may be encumbered with a mortgage. A mortgage provides security for the counterparty's claim, providing a right to satisfy it out of the encumbered immovable. A mortgage contract must be notarised and the mortgage is entered into the Land Register. The owner of the immovable may freely transfer the immovable encumbered with a mortgage, whereas the mortgage stays with the immovable.

# Latvia

## **Registration**

All immovable property including any encumbrances (e.g., mortgages, easements) must be registered with the Land Book Registry. The Land Book Registry is a publicly accessible court register of immovable property.

## **Movable and immovable property**

According to Latvian Civil Law, immovable property is property which may not be moved without external damage from one location to another (land and any building firmly attached thereto).

## **Acquisition**

Under Latvian law, land may be owned without limitation in urban areas by:

- Latvian citizens and EU citizens;
- The state and local governments and their companies;
- Religious organisations registered before 21 July 1940;

- The State's and local governments' higher education establishments;
- Companies registered in Latvia or in any EU country provided that:
  - more than half of the share capital is owned by Latvian or EU citizens, the state or local governments,
  - more than half of the capital is owned by individuals or legal entities resident in countries with which Latvia has signed investment protection treaties enacted before 31 December 1996 (i.e. Finland, Sweden, Denmark, France, Norway, Taiwan, Switzerland, Germany, Poland, Great Britain, Israel, the Netherlands, the Czech Republic, Austria, USA, Canada, Vietnam, Estonia, Lithuania). This applies also to individuals or legal entities from states with which these treaties are signed after 31 December 1996, if these treaties provide the rights of Latvian individuals and legal entities to acquire land in the relevant state (for example, this applies to the Korean Republic),
  - more than half of the capital is owned by a combination of the aforementioned categories of persons,
  - a public joint stock company listed on the stock exchange.

In rural areas land may be owned without limitations by:

- Latvian citizens;
- The State and local governments and their companies;
- Latvian registered religious organisations acting for not less than three years;
- State and local government higher education establishments;
- Farm or proprietorship, owned by a Latvian citizen;
- Public joint stock company (public limited liability companies) listed on the stock exchange;
- A company registered in Latvia provided that:
  - more than half of the capital is owned by a Latvian citizen, the state or local governments
  - more than half of the capital is owned by individuals or legal entities resident in countries with which Latvia has signed investment treaties enacted until 31 December 1996 (i.e. Finland, Sweden, Denmark, France, Norway, Taiwan, Switzerland, Germany, Poland, Great Britain, Israel, the Netherlands, the Czech Republic, Austria, USA, Canada, Vietnam, Estonia, Lithuania). This applies also to individuals or legal entities from states with which these treaties are signed after 31 December 1996, if these treaties provide the rights of Latvian individuals and legal entities to acquire land in the relevant state (this applies to the Korean Republic),

- more than half of the capital is owned by a combination of the aforementioned categories of persons.

EU citizens and legal entities may not obtain rural land until 2011, except:

- If they operate as a self employed farmer and, for at least 3 years, have been residing and actively occupying themselves with agriculture. Forest land is not included.

As of 1 May 2011, after the expiration of the transitional period, EU citizens and legal entities registered in the EU will be able to own land in rural areas under the same conditions as Latvian citizens. If, however, by 1 May 2011, it becomes apparent that serious disturbances to the agricultural land market might occur, the transitional period may be extended by a maximum of 3 years.

Individuals and legal entities not mentioned above may acquire land subject to the local government's consent. However, these individuals are prohibited from acquiring land situated:

- On the Latvian border
- In the protected coastal and other protected zones near public bodies of water
- In agriculture and forestry areas.

## **Real estate contracts**

Contracts for sale and purchase of real estate must be executed in writing (notarisation is not necessary). To register a change of ownership, a notarised request to the Land Registry must be submitted together with the respective contract. If the transaction is not registered with the Land Registry, it is still a legal purchase but the purchaser may not transfer the title or use other rights which may belong to the property owner until registration has taken place.

The stamp duty for transfer of property rights is usually 2% of the value of the property.

## **Mortgage**

A mortgage gives rights to the creditor only after the mortgage is registered with the Land Registry. The mortgage agreement does not have to be notarised. A request to register the mortgage only needs to be signed by the property owner but it must be notarised. A mortgage allows the creditor to sell the collateral by auction, according to rules approved by the court, if the debtor fails to fulfil its obligations.

# Lithuania

## Registration

Real estate (including land plots, buildings, apartments, other premises) and the rights pertaining to it (such property rights as ownership, long-term lease, right of use, servitude, etc.) as well as legal encumbrances on property rights to real estate, including transactions and decisions affecting the legal status of the real estate, testamentary dispositions, and arrests, must be registered with the Real Estate Cadastre and Register. There is no separate register for land in Lithuania.

The conclusion of real estate sale-purchase, rent, etc. contracts and ownership rights shall be enforced against third parties if it has been registered with the public register. Moreover, according to the Lithuanian Civil Code if the party of the agreement avoids registering transfer of ownership rights, the court may act to compensate the losses of the other party.

## Movable and immovable property

The Lithuanian Civil Code distinguishes real estate and movable property. Immovable property is land and other things related to land, which cannot be moved from one place to another, not changing the purpose thereof or essentially decreasing its value, i.e. if they are deemed to be as such due to their purpose and nature. Immovable property also includes ships and aircraft, which are required to be registered with the public register. The laws may also recognise other things as immovable property.

Movable things are the ones that can be transferred from one place to another without any damage, unless the laws provide otherwise.

## Acquisition

In Lithuania, land may be owned by the following persons:

- citizens of the Republic of Lithuania
- the state and municipalities
- domestic and foreign legal persons engaged in economic activity in Lithuania, as well as foreign natural persons.

Foreign legal persons intending to acquire land must comply with the criteria established by the laws, i.e. the foreign entity must be incorporated in an EU, OECD, or NATO member country, or in a country which has concluded an association agreement with the EU.

Foreign legal persons that do not meet the aforementioned criteria may lease the land for up to 99 years. The land may be acquired for the construction of buildings which are necessary for business activity. State-owned land may be leased with or without an auction. The auction should be held in all cases, except for land which bears constructions or facilities owned or leased by private persons.

Foreign natural and legal persons meeting the aforementioned criteria may only acquire ownership of non-agricultural and non-forest land. However, this restriction, which shall be valid until 1 May 2011, does not bind foreigners permanently residing in Lithuania for at least three years, if the entire time they were engaged in agricultural activities, nor does it restrict foreign legal persons having established representative offices or branches in Lithuania.

There are no specific requirements for foreigners to acquire the ownership of real estate other than land.

## **Real estate contracts**

Contracts on the selling and purchasing of real estate shall be executed in writing and approved by the notary public. Failure to notarise such agreements makes them null and void. The mandatory part of a land transaction is a plan of the land plot approved by the competent state authority. The legal title to the real estate is deemed to be passed at the moment the property transfer has been accepted.

The agreement on sale-purchase of real estate must specify the rights of the buyer in respect of the land whereon the real estate is located. If the seller of the real estate is the owner of the land plot attached to the real estate to be sold, the ownership right must be transferred to the buyer according to the sale-purchase agreement. If the owner of the real estate does not hold the ownership right to the land plot concerned, the real estate may be sold without the consent of the land owner only if it does not contradict the conditions of usage of the land as established by the laws and/or an agreement on use of land. Land issues are to be defined in the sale-purchase agreement.

Contracts on leasing real estate must be concluded in writing if the lease term exceeds one year.

Contracts on selling, purchasing or leasing real estate may be enforced against third parties if such contracts are registered with the Real Estate Cadastre and Register.

The fee for notarisation of a sale-purchase contract is 0.5% of the value of real estate (i.e. sales price). The stamp duty for registration of the ownership rights depends on the value of real estate, the owner (state or private person), the purchaser (individual or legal entity) and may range from LTL 20 (approx. EUR 6) to LTL 10,000 (EUR 2,900).

## Mortgage

Mortgages can be seconded on real estate registered with the public register and not excluded from civil use. Only insured property may be mortgaged. Real estate mortgages must be executed on the standard mortgage deed form and approved by the notary public. Real estate mortgages are only effective after the registration thereof with the relevant state register, the Hypothec office at the local court. Upon transfer of the mortgaged property, the mortgage follows the property.



## Chapter 8

# Other legal considerations

## Estonia

### Competition law

The first Estonian Competition Act was already in effect as early as 1993. Today, the Competition Act has gone through various amendments to bring it in to line with the requirements demanded by Estonia's accession to the EU. Due to accession, the regulations of the Council of Europe and the European Commission have a direct impact on Estonian enterprises.

#### Anti-competitive agreements

Agreements, concerted practices and decisions by associations of enterprises, which have the restriction of their object or effect, are prohibited. Above all, the prohibition covers such cooperation between the enterprises by which:

- prices or other essential transaction conditions in respect of other enterprises or clients acting in the market are fixed, or information restricting competition is exchanged
- product market, technical development or investments are limited or controlled
- product markets and supply sources which are shared or accessed by third persons to a product market are restricted
- dissimilar conditions are applied to equivalent agreements or entry into an agreement is subject to acceptance by the other party of obligations which have no connection to the subject of such agreement.

#### Abuse of dominant position

For the purposes of the Competition Act, an enterprise in a dominant position is an enterprise which accounts for at least 40% of the turnover in the product market or whose position enables it to operate in the market independently of other participants

(competitors, suppliers, or clients). In addition, enterprises in a dominant position include those with special or exclusive rights or those in control of essential facilities.

Any direct or indirect abuse by a company or several companies in the dominant position in the goods market is prohibited, including:

- directly or indirectly imposing unfair purchase or selling prices or other unfair trading conditions;
- limiting production, service, goods markets, technical development or investment;
- offering or applying dissimilar conditions to equivalent agreements with other trading parties, thereby placing some of them at a competitive disadvantage;
- making entry into an agreement subject to acceptance by the other parties of supplementary obligations which have no connection with the subject of such agreement;
- forcing a company to concentrate, enter into an agreement which restricts competition, engage in concerted practices or adopt a decision together with the company or another undertaking;
- unjustified refusal to sell or buy goods.

State aid which distorts competition, i.e. any advantage granted by the state or a local government or through their resources, is prohibited in so far as this affects trade between the EU member states.

### Concentration control

Concentration is a merger of enterprises or parts of the enterprises, or acquisition by an enterprise or enterprises, or of control over the whole or part of another enterprise or enterprises (on certain conditions, a natural person may also be the acquirer of control).

Any concentration must be reported to the Estonian Competition Board if the aggregate turnover of the involved parties within Estonia exceeds EEK 100 million and the aggregate turnover in Estonia of each of at least two involved parties exceeds EEK 30 million.

### Liability

Upon the first occurrence of the violation of the rules applicable to enterprises holding dominant position (or rules applicable to enterprises with special or exclusive rights), the prescribed administrative punishment for the members of the governing bodies of such an undertaking is a fine of up to EEK 18 thousand (approx. EUR 1,100) or detention, and for the undertaking itself, a fine of up to EEK 500 thousand (approx. EUR 32,000).

The same punishment is prescribed for the first-time failure to comply with the notification rules regarding concentration.

A second violation of the aforementioned rules is punishable as a criminal offence.

Entering into agreements which have restriction of competition as their intentions or their effect, as well as such concerted practices and decisions, are treated as a criminal offence upon the first instance.

Estonian law allows both an individual and a legal person to be punished for a crime. Criminal punishment for competition offences for a member of a governing body is a fine or imprisonment for up to 3 years. For a legal person, a fine of up to EEK 250 million (approx. EUR 16 million) is prescribed.

Proprietary or other damage caused by acts prohibited by the Competition Act shall be subject to compensation by way of civil procedure.

## **Intellectual property**

The main acts governing intellectual property are the Copyright Act (effective 1992) which regulates both copyright and rights related to copyright, The Patents Act (effective 1994), the Trademark Act (effective 2004), the Utility Models Act (effective 1994), the Industrial Design Protection Act (effective 1998) and the Geographical Indication Protection Act (effective 2000). These regulate industrial property rights. Business names and trade secrets are regulated by the Commercial Code (effective 1995) and the Competition Act (effective 2001).

Estonia is also a signatory to several international treaties. The most important are the Berne Convention for the Protection of Literary and Artistic Works (re-acceded 1994), the Paris Convention for the Protection of Industrial Property (re-acceded 1994), the Geneva Act of the Hague Agreement Concerning the International Registration of Industrial Designs (acceded 2003), and the Convention establishing the World Intellectual Property Organization (acceded 1994). Estonia's intellectual property acts are also consistent with corresponding EU provisions.

## **Consumer protection**

The protection of consumer rights on the legislative level dates back more than 15 years when the first Consumer Protection Act was adopted by the Parliament. Today, the Estonian consumer protection regulations have been brought in line with the EU consumer protection policies and the UN guidelines and the numerous acts in that field, the Consumer Protection Act, the Law of Obligations Act, Trading Act, Advertising Act, Food Act and Product Safety Act, can be considered as the main acts regulating consumer protection in Estonia.

The currently effective Consumer Protection Act entered into force in 2004. The Consumer Protection Act sets forth the fundamentals of consumer protection, including

information requirements, general regulations on the sale of goods and services to consumers and the organisation of consumer protection.

The national authority with the main task of protecting the legitimate interests of consumer is the Estonian Consumer Protection Board. According to the consumer protection policy of the UN and the EU, and also arising from the Consumer Protection Act, the Consumer Protection Board provides the protection of the interests and legal rights of single consumers (not legal manufacturers or entrepreneurs).

## **Anti-money laundering**

The currently effective Money Laundering and Terrorist Financing Prevention Act became effective on 28 January 2008. The purpose of the new wording is to harmonise the Estonian law with the Third Directive (Directive 2005/60/EC of the European Parliament and of the Council on the prevention of the use of the financial system for the purpose of money laundering and terrorist financing that repealed Directive 91/308/EEC) and Directive 2006/70/EC laying down implementing measures for the Third Directive.

The central issue of the new Money Laundering and Terrorist Financing Act is updated due diligence measures that are the primary means for achieving the aims of the act.

The authority primarily responsible for the preventive activities set forth in the law is the Estonian Financial Intelligence Unit (FIU) which is an independent structural unit of the Central Criminal Police. Other authorities, e.g. the Financial Supervisory Authority, The Estonian Bar Association and the Chamber of Notaries, are also involved in the supervision of the adherence to the requirements set forth in the money laundering prevention regulations.

## **Litigation and arbitration**

The Estonian court system consists of three levels. The first instance is formed by four county courts and two administrative courts. Appeals against decisions of courts of first instance are heard by three courts of second instance (sometimes also called circuit courts) situated in Jõhvi, Tartu and Tallinn. The Supreme Court, situated in Tartu, is the court of the highest instance. A matter is heard in the Supreme Court only after all previous court instances have been passed. The filing of an appeal is governed by codes of court procedure.

The decisions of courts of first and second instances are made public in full in the database of court statistics and court decisions. All reasoned judgements of the Supreme Court are published in Part III of the State Gazette and are electronically available on the homepage of the Supreme Court.

The only permanent arbitration court in Estonia is the Arbitration Court of the Estonian Chamber of Commerce and Industry, which settles disputes arising from contractual and other civil law relationships, including foreign trade and other international economic relations. The arbitration court will accept disputes for settlement if parties have voluntarily chosen that the dispute should be settled in the arbitration court or it is so provided by the International conventions.

## Latvia

### Competition law

The Competition Law is the main national legislative act that regulates competition issues in Latvia. The Law came into force on 1 January 2002 and has been amended three times, most recently in November 2008. The Law is in line with EU policies on the regulation of anti-competitive behaviour. The Competition Council supervises this field.

Agreements with the intention of restricting competition are prohibited and therefore are null and void from the moment of being entered into. This includes agreements regarding the fixing of prices and tariffs, restriction or control of the scope of business activities, investment, and the division of markets, the application of unequal provisions in equivalent transactions with third persons, and other types of agreements.

The Law gives examples of exceptional cases when the Competition Council may allow such agreements.

Any competitor having a dominant position in the market is prohibited from abusing its position in any manner within the territory of Latvia. Examples of abuse of dominance might include refusal to enter into transactions with other competitors, restriction of the amount of business activities without proper reason, imposing additional obligations not related to a particular transaction on competitors, application of unequal provisions in equivalent contracts with other competitors, and creating disadvantageous conditions.

The concentration control is overseen by the Competition Council and with the latest amendments of the Competition Law, strict criteria in this regard have been introduced. Consequently, prior to a merger, competitors must submit a notification of their proposed merger to the Competition Council, if the turnover of the competitors exceeds LVL 25 million and each of them has a turnover of at least LVL 1,5 million.

For Competition Law purposes, the concept of "concentration" includes the merging of two or more independent competitors in order to become one competitor (the consolidation), the joining of one competitor to another competitor (the acquisition), and a situation where one or more competitors acquire a decisive influence over another one or more competitors.

If a competitor is found to be in a breach of the provisions of the Competition Law, the Competition Council may impose fines on the competitor of up to 10% of their net turnover for the previous financial year.

In cases of abuse of dominant position, the Competition Council may impose fines of up to 5% of the guilty company's net turnover of the previous financial year. This may be increased to 10% of the violator's net turnover for the previous financial year if the initial fine is not paid.

In situations where there is a violation of the provisions of the law relating to concentrations, a fine of up to LVL 1,000 for each day can be imposed on the new market participant or the acquirer of the decisive influence.

A participant of a cartel notifying the responsible authorities about the cartel is released from responsibility.

## Intellectual property

Latvian legislation provides sufficient legal grounds for enforcement and protection of intellectual property rights complying with principles recognized at the international level. As a WTO (World Trade Organization) member, Latvia participates in the Agreement on Trade-Related Aspects of Intellectual Property Rights (TRIPS). Latvia is a member of the World Intellectual Property Organization (WIPO) and therefore participates in the Paris Convention for the Protection of Industrial Property and the Berne Convention for the Protection of Literary and Artistic Works. An international treaty regulation supplements EU legislation in force.

Trademarks and designs are registered and patents on inventions are granted by the Patent Office. The Patent Office examines the applications for the trademark, design and patent protection and keeps the State Registers.

As a general rule, disputes on protection of the intellectual property rights are subject to the jurisdiction of the Riga district court. Civil procedure law offers effective tools for the protection of intellectual property rights, which may be used even before bringing an action to the court.

In intellectual property cases, evidence may be ensured by a court decision before an action is brought to the court and without summoning potential participants of the lawsuit, if there is a reason to believe that the rights of an intellectual property are being infringed or may be infringed.

If an action is brought to court, the court may, upon a request from the plaintiff, request that the information regarding the origin of the goods or services and the distribution thereof be disclosed by the defendant or other person having such information. The plaintiff may ask for a court decision prohibiting an unlawful use of intellectual property.

The holder of the intellectual property rights may request a court decision on the question of damages and also moral injury compensation for unlawful use of intellectual property.

## Consumer protection

Rights of private persons who are consumers are protected by the government against unfair and dangerous service and goods providers and to help the consumers in choosing goods and services. The sphere of consumer contracts in general is protected, including contracts regarding credits and loans. Contracts concluded by internet (distance contract) also enjoy the protection. There are special regulations that govern the observance of the rights of consumers directly and indirectly (pre-cautionary) to comply with EU directives. The state institution supervising the observance of consumer rights is the Consumer Rights Protection centre.

## Anti-money laundering

Since 13 August 2008, the new Anti-money Laundering Law is in force, which creates strict obligations. The directives of the European Parliament and Council 2005/60/EC, 2006/70/EC are implemented in the new law. Banks, bookkeepers, tax advisers, lawyers, real estate agents etc. must comply with the law. Any other individual who becomes aware of a suspicious transaction is also required to report it. The law implements the "on risk based" principle which means that direct subjects of the law must evaluate the risks of money laundering in their every day activities and, based on this, establish internal policies in order to meet the requirements provided by the international treaties, EC and national law. The Special Supervision office under the prosecutors' office monitors anti-money laundering issues in Latvia.

## Litigation and arbitration

Latvia has a three tier court system. Administrative cases are examined by the Administrative courts. Civil, criminal and other cases are examined by the general courts.

The Regional Court is the court of first instance for most of the cases. Appeals against the Regional Court's decisions are subject to the jurisdiction of a District Court. The District Court is also the court of first instance for some cases of special character. The Supreme Court is located in Riga and has jurisdiction to review petitions for cassation and appeals in cases of special character examined by the District Court as the court of first instance.

If contracting parties have included an arbitration clause in the agreement, the disputes may be subject to the jurisdiction of the arbitration. The courts of arbitration are registered by the Latvian Enterprise Registry. According to the registry there are more than 150 registered arbitration courts in Latvia.

Latvia is a member of the International Chamber of Commerce and Industry. The Arbitration Court of Latvian Chamber of Commerce and Industry (LCCI) provides the

settlement of international and local commercial disputes in accordance to the LCCI Rules of Arbitration and UNCITRAL Arbitration Rules.

The Arbitrator most often cited in contacts used by banks and foreign merchants are the Arbitration Court of the Latvian Chamber of Commerce and the Arbitration Court of the Latvian Commercial Banks Association.

## Lithuania

### Competition law

Competition Law binds Lithuanian commercial activities as well as commercial undertakings registered outside of Lithuania, if the activities of the foreign undertaking limit competition in the Lithuanian market.

Acts of undertakings which are contrary to fair business practices and which have detrimental effects upon the competitive position of other undertakings in the given market are considered as unfair competition and prohibited by law. These acts include: unauthorised use of trade names and trade marks, intentional misrepresentation with respect to products of other undertakings, unauthorised sharing of confidential information about other undertakings, solicitation of employees of other undertakings to leave their job, misleading advertising, etc.

Agreements aimed at restricting competition such as those fixing, directly or indirectly, prices or other sales terms, dividing the market, establishing quantities of production or sales, etc., are prohibited and are deemed legally invalid as of their date of conclusion. Exceptions apply to agreements of insignificant influence which are those between business undertakings whose total market share does not exceed the following limits:

- 10% in the case of horizontal agreements
- 15% in the case of vertical agreements
- 10% in the case of mixed agreements.

"Dominant position" means the position when one or more undertakings can effectively restrict competition through their decisive influence on the market. It is presumed that a person has a dominant position in the market if his market share equals or surpasses 40%, unless it is proven otherwise. Also, each undertaking belonging to a group of three or fewer members with the largest shares in the relevant market, jointly holding over 70% of the relevant market, shall be presumed to have a dominant position, unless it is proven otherwise.



The list of prohibited acts abusing dominant position include unfair pricing, limitations of trade, production or technical development, discriminatory treatment of different groups of undertakings, etc.

Competition regulations also control concentration. The concept of "concentration" includes mergers of undertakings as well as acquisition of control over undertakings.

Concentration is deemed to be controlled if:

- the combined aggregate income of the concerned undertakings for the previous year exceeds LTL 30 million (approximately EUR 8.7 million), and
- the aggregate income of each of at least two concerned undertakings for the previous year exceeds LTL 5 million (approximately EUR 1.5 million).

The controlled concentration must be notified in advance to the Competition Council whose permission is required to perform the concentration.

Any acts implementing the controlled concentration which are performed without having due permission shall be legally void and invalid. The Competition Council may impose fines on undertakings performing the controlled concentration without having due permission. In serious circumstances, fines up to 10% of the annual aggregate income of the undertakings concerned may be imposed.

## **Intellectual property**

The legal regulation on protecting intellectual property in Lithuania is based on the rules and recommendations of the World Trade Organisation and the World Intellectual Property Organisation. Legal acts are in compliance with the EU regulations.

According to Lithuanian law, the object of copyright is defined as original literary, scientific or artistic works that are considered to be the result of creative activity expressed in an objective form. Copyright is not applied to ideas, principles, action methods, intentions, processes, legal acts, official documents, information reports, folk art works, etc.

The law also protects neighbouring rights. The object of neighbouring rights is defined as the performance of works, live or recorded in audio, video tape, phonogram, the first record of audio-visual work, as well as a programme of a radio/television broadcast.

Copyright protection granted by Lithuanian legislation applies to the citizens and permanent residents of the Republic of Lithuania, legal persons having their place of business in the Republic of Lithuania, authors, irrespective of their citizenship and place of residence, who have published works for the first time in the Republic of Lithuania as well as authors of architectural works constructed in the Republic of Lithuania.

The property rights of an author last during the life of the author and for 70 years thereafter. Non-property (personal) rights are protected indefinitely.

In order to be legally protected by Lithuanian law, a trademark must be registered with the State Patent Bureau of the Republic of Lithuania. The registration is not necessary if the trademark is deemed as "well-known" within the meaning of the law.

The registration term of a trademark is 10 years, which may be extended for an additional 10 years an unlimited number of times.

Patent rights belong to inventors, their successors in title as well as to employees for inventions made at work.

Discoveries, scientific theories, mathematical methods, product designs, computer programmes, schemes, and intellectual and economic activities are not regarded as inventions for patent registration.

Know-how and trade secrets are not subject to patent registration, unless they relate to technical inventions (solutions).

For patent protection, inventions must be registered by filing an application with the State Patent Bureau of the Republic of Lithuania or an international application following the international treaty on patent co-operation. The patent protection may also be sought by extending the European patent into the territory of Lithuania. A registered patent is valid for 20 years from the date the relevant application is filed.

Lithuania, being a party to the co-operation agreement with the European Patent Organisation, recognises the priority right with respect to the patent protection granted by foreign countries.

## **Consumer protection**

The fundamental rights of consumers established by Lithuanian law include the right to good quality and safe products and services; the right to information on goods and services as well as information on protection of consumer rights; the right to compensation for a breach of consumer rights; etc. Following the EU pattern, the concept of strict liability is established in Lithuanian legislation.

Quality of goods and services must meet the standards stipulated by law or contract. If the quality does not comply with the standards prescribed, a consumer has the following right to:

- claim for a replacement of the defective goods; or
- claim for a reduction in the price of the defective goods; or
- eliminate the defects at the seller's costs; or
- terminate the sale-purchase contract and to have the purchase price refunded.

A seller is deemed to be responsible for the quality of goods. Goods entering the market must also meet safety requirements.

Legal and natural persons (including producers, importers, distributors, sellers) supplying goods to the Lithuanian market are responsible for proper labelling. Labelling must be in the Lithuanian language and include information about the producer's name, address, country of origin, date of production, etc. Certain categories of goods (e.g. alcohol, tobacco) must have additional labelling with special state-issued labels and must bear warnings on their negative effects to human life and health.

## Anti-money laundering

Lithuania has implemented the Directive 2005/60/EC of the European Parliament and of the Council of 26 October 2005 on the Prevention of the Use of the Financial System for the Purpose of Money Laundering and/or Terrorist Financing.

Money laundering means conversion or transfer of property, knowing that such property is derived from criminal activity, for the purpose of concealing or disguising the illicit origin of the property; concealment or disguise of the true nature, source, location, disposition, ownership of property, knowing that such property is derived from criminal activity, the acquisition, possession or use of property, knowing at the time of receipt/transfer, that such property was derived from criminal activity, help in the commission of any of the activities mentioned.

Reporting obligations are assigned to financial institutions and other entities such as auditors; insurance undertakings; bailiffs; undertakings providing accounting or tax advisory services; notaries; advocates when they are acting on behalf of customer and by assisting the customer in the execution of transactions concerning the buying or selling of real property or business entities, the managing of customer money, securities, the opening or management of a bank, savings or securities accounts, trust or other corporate service providers; persons engaged in trade in immovable properties, precious metals, cultural goods, antiques or other assets the value of which exceeds EUR 15,000 and the payments are made in cash; companies organising gaming; postal services providers; and close-ended investment companies.

Financial institutions and other entities must take all the measures to identify the customer and the beneficial owner when establishing a business relationship, when concluding transactions amounting to more than EUR 15,000, when exchanging cash, when the amount exchanged exceeds EUR 6,000, or in any other case when there are suspicions that the activities of money laundering or terrorist financing is, has been or will be performed.

Financial institutions, performing a monetary operation, must submit to the Financial Crime Investigation Service data confirming the customer's identity and information about the performed monetary operation, if the total amount of the customer's single operation in cash or of several interrelated operations in cash exceeds EUR 15,000, subject to certain exemptions provided by the law.

In certain cases simplified verification of a customer's identity can be performed.

## Litigation and arbitration

The Constitution of the Republic of Lithuania provides that the courts have the exclusive right to administer justice.

The Lithuanian system of general jurisdiction courts consists of the Supreme Court (1), the Court of Appeals (1), district courts (54) and regional courts (5) dealing with civil and criminal cases. Administrative litigation is assigned to the Highest Administrative Court (1) and regional administrative courts (5).

A district court is first instance for criminal cases, civil cases and cases of administrative offences (assigned to its jurisdiction by law), cases assigned to the jurisdiction of mortgage judges, as well as cases relating to the enforcement of decisions and sentences. Judges of a district court also perform the functions of a pre-trial judge or an enforcement judge.

Administrative courts hear disputes in the field of public administration, deal with issues relating to the lawfulness of regulatory administrative acts, tax disputes, etc. Before applying to an administrative court, individual legal acts or actions taken by entities of public administration provided by law may be disputed in the pre-trial procedure.

There is also the Constitutional Court which determines whether the laws and other legal acts are in conformity with the Constitution or whether the decisions of the president and resolutions of the government conform to the Constitution and laws.

The concept of precedent law is not applicable in Lithuania; however the Senate of the Supreme Court is analysing the court practice and adopting recommendations on the uniformity of legal interpretations.

The Lithuanian Law on Commercial Arbitration is applied both for national and international arbitration. National arbitration is defined as arbitration to resolve disputes between economic entities of the Republic of Lithuania except for the disputes referred to international arbitration (e.g. parties have their place of business in different countries; the place of arbitration is outside the country in which the parties have their places of business; parties have expressly agreed that the subject matter of the arbitration agreement is related to more than one country; one or both parties to the dispute are Lithuanian economic entities in which foreign capital is invested, etc.).

Commercial dispute is defined as a controversy between the parties arising from contractual or non-contractual legal relations, except for the disputes which, subject to the law, cannot be submitted to arbitration. Disputes arising from constitutional, employment, family, administrative legal relations, as well as disputes connected with competition, patents, trademarks or bankruptcy agreement cannot be submitted to arbitration.

Arbitrational agreement shall be expressed in writing and it may be in the form of an arbitration clause in an agreement or a separate agreement can be concluded by the parties. The parties are free to determine the number of arbitrators. Failing such determination, the number of arbitrators shall be three.

Both institutional and ad hoc arbitrations are recognised in Lithuania. Arbitral award is binding to the parties at the moment it is made. The parties no longer have the right to start action concerning the same subject matter based on the same grounds. Arbitral awards are enforced under the same procedures as court rulings. Foreign arbitral awards made in the country which is a party to the New York Convention are recognised and enforced in Lithuania. Recognition and enforcement of foreign arbitral awards is carried out through the Lithuanian Court of Appeals.

## Appendix A

# Tax treaties

## Estonia

As of 1 January 2009 Estonia has effective tax treaties with the following countries:

Armenia	Latvia
Azerbaijan	Lithuania
Austria	Luxembourg
Belarus	Malta
Belgium	Moldova
Bulgaria	The Netherlands
Canada	Norway
Czech Republic	Poland
China	Portugal
Croatia	Romania
Denmark	Singapore
Finland	Slovakia
France	Slovenia
Georgia	Spain
Germany	Sweden
Greece	Switzerland
Hungary	Turkey
Iceland	Ukraine
Ireland	United Kingdom
Italy	USA
Kazakhstan	

# Latvia

In 2009 Latvia has effective tax treaties with the following countries:

Albania	Lithuania
Armenia	Luxembourg
Austria	Malta
Azerbaijan	Macedonia
Belarus	Moldova
Belgium	Montenegro
Bulgaria	Norway
Canada	Poland
China	Portugal
Croatia	Romania
Denmark	Serbia
Estonia	Singapore
Finland	Slovakia
France	Slovenia
Georgia	Spain
Germany	Sweden
Greece	Switzerland
Czech Republic	The Netherlands
Hungary	Turkey
Italy	UK
Iceland	Ukraine
Ireland	United Kingdom
Israel	USA
Kazakhstan	Uzbekistan
Kyrgyzstan	

# Lithuania

In 2009 Lithuania has effective tax treaties with the following countries:

Austria	Latvia
Armenia	Luxembourg
Azerbaijan	Macedonia
Belarus	Malta
Belgium	Moldova
Bulgaria	Netherlands
Canada	Norway
China	Poland
Croatia	Portugal
Czech Republic	Romania
Denmark	Russia
Estonia	Singapore
Finland	Slovakia
France	Slovenia
Germany	South Korea
Georgia	Spain
Greece	Sweden
Hungary	Switzerland
Iceland	Turkey
Ireland	Ukraine
Israel	United Kingdom
Italy	USA
Kazakhstan	Uzbekistan



## Appendix B

# Useful links

## Estonia

Parliament of Estonia	<a href="http://www.riigikogu.ee">www.riigikogu.ee</a>
Estonian legal acts in English	<a href="http://www.legaltext.ee">www.legaltext.ee</a>
Bank of Estonia	<a href="http://www.eestipank.info">www.eestipank.info</a>
Ministry of Justice Centre of Registers	<a href="http://www.eer.ee">www.eer.ee</a>
Ministry of Finance	<a href="http://www.fin.ee">www.fin.ee</a>
Financial Supervision Authority	<a href="http://www.fi.ee">www.fi.ee</a>
Estonian Tax and Customs Board	<a href="http://www.emta.ee">www.emta.ee</a>
Ministry of Finance	<a href="http://www.fin.ee">www.fin.ee</a>
Estonian Auditing Board	<a href="http://www.auditorkogu.ee">www.auditorkogu.ee</a>
Estonian Labour Market Board	<a href="http://www.tta.ee">www.tta.ee</a>
Ministry of Social Affairs	<a href="http://www.sm.ee">www.sm.ee</a>
Ministry of Justice Centre of Registers	<a href="http://www.eer.ee">www.eer.ee</a>
Estonian Patent Office	<a href="http://www.epa.ee">www.epa.ee</a>
Estonian Competition Board	<a href="http://www.konkurentsiamet.ee">www.konkurentsiamet.ee</a>
Financial Supervision Authority	<a href="http://www.fi.ee">www.fi.ee</a>
Tallinn Stock Exchange	<a href="http://www.ee.omxgroup.com/">www.ee.omxgroup.com/</a>
Estonian Central Register of Securities	<a href="http://www.e-register.ee/">www.e-register.ee/</a>

## Latvia

Latvian Investment and Development Agency	<a href="http://www.liaa.gov.lv">www.liaa.gov.lv</a>
Bank of Latvia	<a href="http://www.bank.lv">www.bank.lv</a>
Parliament of Latvia	<a href="http://www.saeima.lv">www.saeima.lv</a>
Cabinet of Ministers	<a href="http://www.mk.gov.lv">www.mk.gov.lv</a>
Ministry of Finance	<a href="http://www.fm.gov.lv">www.fm.gov.lv</a>
Ministry of Foreign Affairs	<a href="http://www.am.gov.lv">www.am.gov.lv</a>
Latvian Embassies Abroad	<a href="http://www.am.gov.lv/en/ministry/mission/">http://www.am.gov.lv/en/ministry/mission/</a>
Ministry of Interior Affairs	<a href="http://www.iem.gov.lv">www.iem.gov.lv</a>
Ministry of Economics	<a href="http://www.em.gov.lv">www.em.gov.lv</a>
State Revenue Service	<a href="http://www.vid.gov.lv">www.vid.gov.lv</a>
Riga Stock Exchange and Latvian Central Depository	<a href="http://www.rfb.lv">www.rfb.lv</a>
Central Statistical Bureau	<a href="http://www.csb.gov.lv">www.csb.gov.lv</a>
Land Register	<a href="http://www.zemesgramata.lv">www.zemesgramata.lv</a>

## Lithuania

Parliament of Lithuania	<a href="http://www.lrs.lt">www.lrs.lt</a>
Bank of Lithuania	<a href="http://www.lb.lt">www.lb.lt</a>
Company Register	<a href="http://www.kada.lt">www.kada.lt</a>
Government of Lithuania	<a href="http://www.lrvk.lt">www.lrvk.lt</a>
Ministry of Finance	<a href="http://www.finmin.lt">www.finmin.lt</a>
Ministry of Foreign Affairs	<a href="http://www.urm.lt">www.urm.lt</a>
State Tax Authority	<a href="http://www.vmi.lt">www.vmi.lt</a>
Lithuanian Chamber of Auditors	<a href="http://www.lar.lt">www.lar.lt</a>
Lithuanian Labour Exchange	<a href="http://www.ldb.lt">www.ldb.lt</a>
Competition Council of Lithuania	<a href="http://www.konkuren.lt">www.konkuren.lt</a>
National Stock Exchange	<a href="http://www.nse.lt">www.nse.lt</a>
State Patent Bureau	<a href="http://www.vpb.lt">www.vpb.lt</a>

## Appendix C

# KPMG in the Baltics

KPMG is one of the leading professional services firms providing Audit, Tax and Advisory services in the Baltic States. This is a swiftly growing practice with offices in Tallinn, Riga, Vilnius and Klaipeda.

KPMG member firms in Latvia, Estonia and Lithuania operate as one business unit under common management. This allows KPMG to coordinate services to a geographically dispersed group with a single point of contact, increasing the efficiency and effectiveness of our services.

We serve clients across all industry sectors, including subsidiaries of large international companies, successful local entrepreneurs, state institutions and agencies, and non governmental organizations.

In October 2007 a KPMG office opened in Minsk. The Belarusian member firm operates under the oversight of KPMG in the Baltics fostering common service standards in the Baltics and Belarus.

Our range of services allows us to meet the expectations of clients who desire multidisciplinary services being provided by professionals who know them:

- **Extensive experience** – KPMG firms have been operating in the Baltics since 1992.
- **Coordinated client support** and consistent high quality of services throughout the Baltics, enhanced by an excellent understanding of the specific features of each country.
- **A professional and dedicated team** with 11 partners and more than 400 professionals actively benefiting from shared knowledge, experience and information in the Baltic region and Belarus.
- **International support** – KPMG in the Baltics is a member of a global network of professional advisory firms which allows us to draw on international know-how and benefit from knowledge sharing.

KPMG in the Baltics and Belarus provide a wide range of high quality services to meet rapidly changing client expectations in the developing markets of the Baltics and Belarus.

# Our services

## Audit

- Audit Related Services:
  - IFRS
  - GAAP Accounting
- Financial Statement Audit
- Statutory Audit

## Tax

### Business Tax

- Corporate & Business Tax
- International Corporate Tax
- Indirect Tax
- Mergers & Acquisitions
- Transfer Pricing
- Global Tax Outsourcing
- Legal Services\*

### Personal Tax

- Taxation Services to Individuals \*\*
- International Executive Services

## Advisory

### Financial Advisory Services

- Corporate Finance
- Forensic
- Restructuring
- Transaction Services

### Risk Advisory Services

- Accounting Advisory Services
- Business Performance Services
- Financial Risk Management
- Internal Audit, Risk and Compliance Services
- IT Advisory

\* *Legal services may not be offered to SEC registrant audit clients or where otherwise prohibited by law.*

\*\* *Taxation services to individuals may not be offered in certain jurisdictions due to legal or regulatory constraints."*

The information contained herein is of a general nature and is not intended to address the circumstances of any particular individual or entity. Although we endeavor to provide accurate and timely information, there can be no guarantee that such information is accurate as of the date it is received or that it will continue to be accurate in the future. No one should act on such information without appropriate professional advice after a thorough examination of the particular situation.

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