Corporate tax across the EU

At present the EU represents a myriad different tax rates and approaches to tax legislation. However, the desire of the EU to create a harmonised system may change this in the future. In the third in our series of comparative pieces analysing the whole of the EU, we look at the differences in corporate tax policy across Europe and discuss the implications of a harmonised system on different Union members.

In the last few years there have been a number of changes in the corporate tax system of Latvia, especially in 2004 when many changes were made in order to harmonise several corporate tax issues with the European Union law.

Since 1st January 2004 the corporate income tax rate in Latvia has been 15% which is one of the lowest corporate income tax rates within the European Union. Some years ago the rate was higher but the government decided to reduce it gradually and thus make Latvia more attractive to foreign investments.

Moreover, besides the low corporate income tax rate Latvia also has a very favourable dividend taxation system. Initially Latvia did not tax dividends paid between companies that were residents in Latvia. Since 1st January 2007 Latvia has applied the same rule also to dividends which are paid out to the company which is resident for tax purposes in another European Union Member State or in a European Economic Area member state. Those companies, besides being residents for tax purposes, should also comply with other criteria such as having one of the legal forms of the companies mentioned in the annex of their EU Parent Subsidiary directive. They should also be payers of corporate income tax in their respective states.

Latvia is one of those EU Member States which provides for group relief of losses. After the well-known judgement by the Court of Justice of the European Communities in the Marks & Spencer case (C-446/03) Latvia has made amendments in its corporate tax law and now the group relief of losses is also extended to the foreign companies that are residents in states with which Latvia has a double tax treaty, and to companies that are residents in other European Economic Area member states (Iceland, Lichtenstein and Norway). Thus there is no discrimination between residents and non-residents.

At the moment only a few corporate income tax issues have been harmonised at the EU level, and EU member states are very eager to keep their sovereignty in direct tax areas. There are still a lot of differences between different national corporate tax systems. It could be said that there exists a competition between different member states` tax systems within the European Union. The existence of different corporate tax systems provides companies with the opportunity to choose and to use different advantages offered by the various national corporate tax systems. However, at the same time, those differences in some cases, especially in the case of small and medium companies, hinder companies engaging in cross-border activities as they are not able to deal with all the specific demands of each tax system.

There are many different interests to consider in this area. On the one hand, interests of different member states which are not satisfied that their tax sovereignty is becoming more limited, especially with the activities of the Court of Justice of the Communities in direct tax area.

In our view, it is very important for all interested parties to establish the equilibrium between those interests and create legal certainty in order to facilitate development and smooth functioning of the EU internal market.

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