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GES NewsFlash

Lithuania – New Treatment of Income in Kind and Employer's Allowable Deductions for CIT Purposes

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Summary

The new principles of taxation of income in kind came into force on 1 January 2010 upon amendment of the Law on Personal Income Tax (PIT). The list of benefits for individuals to be considered as taxable income in kind was significantly expanded.

At the same time, provisions of the Law on Corporate Income Tax (CIT) were amended, and the list of benefits provided to employees considered as allowable deductions of employer (company) for CIT purposes was expanded as well.

Income in kind – new treatment starting 1 January 2010

Before the mentioned changes, the Law on PIT provided for an explicit list of what is considered as income in kind, and since 1 January the Law also lists what is not deemed income in kind. It follows that anything that falls under the definition of income in kind and is not included in the list of exceptions, should be considered as taxable income in kind.

Generally, benefits in kind received by an individual from employer are subject to taxes as monetary remuneration (exceptions apply).

The underlying changes in the regulation of income in kind are related to the private use of company cars, receipt of loans with preferential interest, stock options, etc.

Private use of a company car

If an employee has a possibility to use company car for private purposes, e. g. may use the vehicle on weekends and similar, based on the provisions of the new regulations, such employee is deemed to have received income in kind.
Income in kind resulting from the private use of the company car may be evaluated using one of the two methods:

- The first method assumes that income in kind corresponds to 0.75% of the vehicle market price per month. In this case, it is irrelevant how often or how long the car is actually used.
- The second method refers to the calculation of income in kind based on the actual market value of the rent of the car. In this case, the actual use of company car for private purposes has to be taken into account.

According to the recent explanations of the Tax Authorities, fuel expenses covered by an employer fall within income in kind calculated as mentioned above, i.e. expenses covered by employer for private trips of employees are not considered as separate income in kind. Should the employer not pay for fuel for private trips of employees (they pay themselves), then it is assumed that income in kind corresponds to 0.7% of the vehicle market price per month instead of the abovementioned rate of 0.75%.

A rather common case when an employee grants the employer a right to use his/her private car (agreement for use) or leases it but, however, retains a right to use the car for private purposes. In case the employer bears the cost of maintenance, repair or insurance, the share of such costs corresponding to the private use of the car will be treated as income in kind.

Deloitte's View

It should not be understood that the use of a company car results in income in kind by default. In case the employer does not grant the employee a right to use company car for private purposes, e.g. the vehicle is used for business purposes only and is kept in the company outside the working hours, the employee does not receive any income in kind.

Should the employer not provide employees with such benefit as personal usage of a business car, it should prepare necessary documents (e.g. internal policy) and implement the policy where the employees do not have such right. In such case the employees should not be deemed as provided with income in kind in this respect. However, formal prohibition may not be sufficient, if it appears that factually the vehicle is used for private purposes. In such cases the employee would nevertheless be deemed to have received income in kind as substance over form principle is applied in Lithuanian tax practice.

Loans with preferential interest rate

When an individual receives a loan with preferential interest rate, i.e. pays lower interest than would be in the market or no interest at all, he/she is deemed to have received income in kind. The value of income in kind in this case is equal to the difference between the interest that would be paid in the market and the interest that

was actually paid.

There is one exception available to the employees who received a preferential loan to acquire or to build housing before 1 January 2009. In such case, no income in kind is recognized. However, if the mentioned loan was received after 1 January 2009, the difference between market interest and the actually paid interest rates is treated as income in kind.

Stock options

As a popular motivation tool, employers provide employees options to acquire stocks of the company. Before the adoption of the new rules, no income was recognized for the employee upon receipt of securities (e.g. shares) free of charge or for a lower price than market level. Taxes were due only upon further sale of such securities.

With the new rules, the advantages of this motivation tool are lost, because taxable moment is the moment of exercise. The taxable value is the market value of the shares being granted.

Employer's allowable deductions for Corporate Income Tax purposes as from the tax year of 2010

Following amendments of the Law on CIT, calculating taxable profit of 2010 or later years, expenses of a company for the benefit of employees, if such benefit is subject to PIT, are considered as allowable deductions until the tax year of 2010, generally only remuneration for the work performed was considered as allowable deductions.

Deloitte's View

Additional benefits for employees such as subscription to a sports club, payment for trainings or classes of employees that generally does not relate with his functions in the company or activities of the company, etc. can now be attributed to allowable deductions for CIT purposes. On comparison, until the tax year of 2010 this was not possible, such expenses were considered as non-allowable deductions.

Additionally, starting in the tax year of 2010, benefits to employees or their family members that are not subject to PIT are considered as limited allowable deductions for CIT purposes. However, in case it is not possible to determine the benefit of a particular individual, then the expenses are not considered as allowable deductions or limited allowable deductions if such benefit is not established in the collective agreement of the entity and available for all employees. If it is established in the collective agreement, then such expenses can be deducted up to 5% of remuneration of the employees that is subject to social security contributions.

People to Contact

If you have any questions concerning the issues in this GES NewsFlash, please contact one of the tax professionals as follows:

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