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Registration of business and taxation in Latvia 2016

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Preface

This informative material has been prepared with the aim to provide a general overview of the business environment and taxes in Latvia. The information included is based on Latvian legislation in force on 1 January 2016.

Introduction to Leinonen Latvia

Leinonen Latvia is all about company formation, accounting and payroll, advisory and audit services for more than twenty years. The company is a part of Leinonen Group - expanding international entity with offices in 11 countries: Finland, Sweden, Norway, Estonia, Latvia, Lithuania, Poland, Hungary, Bulgaria, Russia and Ukraine.

Since 2009 reliability of Leinonen Latvia accounting services have been assured by Bureau Veritas with ISO 9001:2008 Certificate.

Leinonen Latvia is a member of Norwegian Chamber of Commerce, Finnish Chamber of Commerce, Swedish Chamber of Commerce,

American Chamber of Commerce and Latvian Chamber of Commerce and Industry.

For further information on matters described in this publication, please contact Jūlija Bajāre, Country Manager, Leinonen Latvia.

LEINONEN LATVIA

Vilandes iela 3
LV 1010 Rīga
Telephone: 371 67 323 901





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General information about Latvia

*Presented data issued by state institutions concerns year 2015 if not stated otherwise.

Location / boarder countries	Northern Europe, the east coast of Baltic Sea, land: Estonia, Russia, Belarus and Lithuania
Government type	democratic, parliamentary republic
Population	2.3 million (58% Latvian and 29% Russian)
Area	64,573 km ² (44.8% of the territory are forests)
Foreign policy	Membership with EU and NATO since 2004, the euro zone in 2014. Membership with WTO, Schengen Area. Joining OECD planned in 2016
Capital city	Riga (701,185 inhabitants)
Official language	Latvian (it belongs to the Baltic branch of the Indo-European language family)
GDP	24841.6 million. euro
GDP growth	GDP growth of 2.1%
Economically active population	885.9 thousands
Unemployment rate	9.7%
Inflation rate (2014)	0.6%
Main economic sectors	Mechanical engineering, electronics, pharmaceutical production, forestry, wood processing, agriculture, textiles, information technology and telecommunications
Largest ice-free ports	Riga, Ventspils and Liepaja.
Export volume goods & services (2014)	13.96 billion EUR
Import volume goods & services (2014)	14.65 billion EUR
Export products	Machinery equipment, wood, paper products, medicine, textile, food products, furniture, metal, chemical products, vehicles and their parts
Import products	Machinery and equipment, chemical products, textiles, food
Natural resources	Oil shale, peat, clay, limestone, natural sand, dolomite, sea mud, arable land, forest
Key trading partners	Germany, Sweden, the UK, Russia, neighboring Baltic countries Estonia and Lithuania
Education of residents	23% a higher education, 30.2% - secondary or professional education, 23.8% - secondary
E- services	<ul style="list-style-type: none"> -Online communication with state & municipal institutions (declaration of residence, cadastre information system) and e-payments (real estate taxes etc.) - Annual tax declarations, electronic tax returns for economic operators etc. via State Revenue Service system -E-signature via ID card - Online and mobile services i.e., banking transactions, parking fee payments -Latvia has the fastest Internet connections in the world
Banks	Several international banks: Swedbank AS, AS Nordea AB Latvian branch of DNB Bank, SEB Bank operating in the market
Merchant associations	Active public organizations, merchant's associations, international chambers of commerce (Norway, Finland, Sweden, UK, USA, Canada)

1. Registration of economic activity and accounting requirements

1.1 Legal forms

The most common registration forms of entrepreneurial activities are a limited liability company, a joint-stock company and individual merchant. In addition, it is possible to register a branch of foreign company, permanent establishment and the partnership (joint venture). Each of the above forms, except individual merchants pays corporate income tax in accordance with the law "On Corporate Income Tax" or micro enterprise tax as per the Micro-Enterprise Tax Act (for details please see Section 3.2). Individual merchant pays personal income tax as per the law "On Personal Income Tax".

1.1.1 A limited liability company (SIA)

A company may be formed by one or more members i.e., legal or natural persons. A liability of the shareholders is the amount of the share capital. The minimum share capital is 2 800 euro. At least 50% of the share capital must be paid prior company establishment; the balance must be paid up within one year after the registration.

It is possible to establish a low capital company with a share capital of 1 euro. Following criteria should be met:

- Shareholders no more than 5 persons
- The board composed of one or more of the SIA shareholders (persons)
- A shareholder at the same time can be a member only in one low capital company.

1.1.2 A joint stock company

A joint-stock company may be formed by one or more natural or legal persons. Responsibility of shareholders is the amount of registered share capital. The minimum share capital volume is 35 000 euro. At least 25% of the share capital must be paid before the company is established, the balance to be paid within one year after signing the registration contract. The amount of the share capital of credit institutions and insurance companies is higher.

1.1.3 Partnerships

A partnership is one of the legal forms divided into two types - general partnerships and limited partnerships.

The aim of general partnership of two or more persons (members) is to perform commercial activities using joint firm on the basis of contract without limiting their liability against creditors. A limited partnership differs from general partnerships since at least one member (limited partner) liability in respect of the company's creditors is limited to the amount of its contribution. The rest of the personally responsible members of society (complementary) liability are not limited. Amount of partner investment is not limited to a specific amount.

A member of a partnership may be natural or a legal person, as well as other person entitled to legal partnership. Partnerships must be registered in the commercial register.

1.1.4 Individual merchant

Individual merchant is a natural person engaged in economic activity.

Individual merchant is liable for its obligations with all its property. A natural person engaged in an economic activity is obliged to apply to register in the commercial register as individual entrepreneur if the annual turnover from the economic activities exceeds 284 600 euro or the business activities performed comply with both following characteristics:

- 1) The annual turnover from activities exceeds 28 500 euro
- 2) There are more than five employees.

A natural person may apply for registration as the merchant in the commercial register, even in the absence of the above-mentioned conditions.

1.1.5 Branches

The foreign company may establish a branch in order to register an economic activity in Latvia. The branch should be managed by authorized representative of the foreign company. The branch is not considered as a separate legal entity thus a branch founder is responsible for the branch accounts (receivable and payable).

1.1.6 Permanent establishment of foreign company with right of economic activity

A permanent establishment of the foreign company should be registered by the State Revenue Service (SRS) according to location of business in accordance with the procedures governed by Cabinet of Ministers Regulations No. 537 on registration of the taxpayer and the taxpayers' departments within State Revenue Service.

1.1.7 Representative office without right to pursue an economic activity

A foreign company can register its representative office (RO) in Latvia. RO is not allowed to pursue an economic activity. It may engage in only certain support functions, i.e., market research etc.

The procedures for registration of RO of foreign companies are governed by the Cabinet of Ministers Regulation No. 401 and are registered at Latvian Company Register.

1.2 Board members responsibility

The amendments to the Law “On Taxes and Fees” provide that the board members are personally liable for the tax debts of legal entities since 1 January 2015. The liability can be extended to legal persons with late tax payments accrued after 1 January 2015.

The SRS may initiate a process for collection of the delayed tax payments from the board member if following criteria are fulfilled:

- The amount of tax arrears exceeds 50 (fifty) minimum wages (18 000 euro during 2015 and 18,500 euro in 2016)
- Decision on collection of late tax payments has been notified to the taxpayer
- Statement on the tax debt, the taxpayer has disposed the assets to the person concerned
- The decision/act has been attested on impossibility of recovery
- The taxpayer who carries out an economic activity has not fulfilled the statutory obligation to submit application for insolvency proceedings.

If the entity has several Board members, they are jointly liable for late tax payments.

1.3 Accounting requirements

The economic operators should keep records that provide true information on a person’s financial situation. If turnover does not exceed the statutory amount, for example, if revenue of an individual merchant from economic transactions does not exceed 300 000 euro in the previous fiscal year a single entry accounting is permitted.

In general, the accounting must be carried out in accordance with Latvian law. In certain cases, for credit institutions, insurance companies etc., the accounting must comply with International Accounting Standards.

Accounting records should be in Latvian and in euro. The accounting documents should be stored in Latvia, the storage period is 10 years, except for wages, accounting documents must be kept for 75 years.

The annual report and its annexes must be prepared in Latvian for submission to SRS within one month following the approval and not later than four months after the end of year. For the medium sized company, a large company and the parent company which prepare the consol-

idated annual accounts the annual report must be submitted no later than seven months after the end of year.

Micro enterprise is a small size company not exceeding two of three thresholds below at the balance sheet date:

- 1) Balance sheet total - 350 000 EUR
- 2) The net turnover - 700 000 EUR
- 3) The average number of employees for a year –10.

Small size companies are those not exceeding two of three thresholds below at the balance sheet date:

- 1) Balance sheet total - 4 000 000 EUR
- 2) Net sales - 8 000 000 euro
- 3) The average number of employees for the year – 50.

A medium sized company is not exceeding two of three thresholds below at the balance sheet date:

- 1) Balance sheet total - 20 000 000 euro
- 2) Net sales - 40 000 000 in the euro
- 3) The average number of employees for the year – 250.

A company exceeding two of three thresholds of a medium size company at the balance sheet date is a large company.

2. Employment in Latvia

2.1 General employment requirements

The Latvian labour law sets minimum employment requirements including equal pay for work of men and women, amount of minimum wage, entitlement for paid leave etc.

Prior employment, the employee and the employer must sign a written employment contract. According to the Labour Law the employment contract must contain the following information:

- The employee's name, address and personal identification number
- The employer's name, address and registration number
- Commencement date
- Place of work, position and duties to be carried out
- The salary amount and date of payment
- Working hours
- Duration of paid annual leave

- The notice period for termination of the employment contract.

An employee has the right to terminate the employment contract in written one month in advance in case shorter notice period is not specified in the collective agreement and / or the employment contract. Upon request of the employee, temporary incapacity for work is not eligible during the notice period.

The employer has the right to terminate the employment contract due to the conduct of the employee, the ability to perform duties or economic, technological and other reasons in a company.

Working conditions can be defined in the collective agreement. The collective agreements are signed by the employer and trade unions or other employee who is approved as authorized

representative. Joining a trade union is possible on a voluntary basis.

The minimum wage in 2016 is 370 euro (40 hour working week). The minimum hourly rate as of 2016 is calculated according with formula set by the Cabinet of Ministers regulations and is based on the minimum wage and the normal working hours per month.

2.2 Visas and residence permits

Citizens of European Union and European Economic Area countries do not require visas to enter the Republic of Latvia. Certain other third countries can visit Latvia without visa for a period not exceeding 90 days within 180 days' period. Other third country nationals can visit Latvia after obtaining a short term, long term or transit airport visas.

Citizens of foreign countries willing to work as employees or self-employed persons in Latvia require working visa or work permit.

Temporary or permanent residence permit is required for person willing to stay in Latvia for more than 90 days during six-month period.

For more information on visas and permits, please visit following site: <http://www.pmlp.gov.lv/en/home/services/visas-and-invitations/#1>

2.3 Social benefits and pension system

Having paid the state compulsory social insurance, it includes the following:

- State pension
- Unemployment
- Insurance against accidents at work and occupational diseases
- Disability
- Maternity and sickness
- Parental insurance.

Sickness benefit for the employee's illness period should be covered by the employer from its own funds following 75% of the average earnings for 2nd and 3rd temporary disability days and 80% for the period from the 4th day of incapacity to 10th day inclusive. There is no sickness benefit for the 1st day of temporary incapacity.

Sickness benefit to the insured person is paid starting from 11th day of sickness from the social security budget. The sickness benefits for

child up to age of 14 are paid for a period from 1st day to 21st day of incapacity for work and including the entire period of maternity leave.

Retirement pension for residents in Latvia is entitled for persons reaching the age of 65. For persons born between 1952 and 1960 the retirement age is 62 to 64.75 years depending on the year of birth.

2.4 Employment income - personal income tax, state social insurance compulsory payments and solidarity tax

2.4.1 Personal income tax rate and exemptions

Personal income tax rate is 23%.

The amount of relief for the dependent is 175 Euros a month. Annual minimum non-taxable is 75 euro per month. In addition, as of 2016 tax year, there is differential non-taxable income depending on the total annual income of the person. The taxable income of the person may be

reduced by payments into private pension funds and for life / health insurance premiums. The person should submit an annual tax declaration in order to obtain a refund of overpaid tax.

The employer's premium payments for employee life insurance (including accumulation of funds) which do not exceed 10% of the gross wage for a tax year and life (without accumulation of funds), health and accident insurance premiums paid for an amount not exceeding 10% of the taxpayer calculated gross wage during tax year but not more than 426.86 Euros per year are not taxed if legislative provisions are met.

The employee income from share purchase is tax exempt upon fulfilment of following conditions:

- 1) the minimum retention period of share purchase rights is not less than 36 months from the share purchase award till a date when the employee is entitled to initiate a share purchase rights
- 2) the employee is employed by the capital company granting the taxpayer the share purchase rights or a company as per the law "On Corporate Income Tax" has granted the taxpayer the share purchase rights during retention period of the share purchase rights i.e., from the share purchase award date till the share purchase date

3) employer has submitted the information stated in the Law "On Personal Income Tax" to the SRS.

The employer's benefits to employees i.e., gifts exceeding 14,23 Euro in the tax year, housing and other benefits are all taxable.

2.4.2 Compulsory social insurance contributions from employment income

Compulsory social insurance contributions should be made from the gross employment income. The maximum amount i.e., „ceiling" of social contribution is 48,600 euro in a calendar year.

In general, the employer's contribution rate is 23.59% of the employee's gross income; the employee's contribution rate is 10.5% which is deducted from the employee's income. For certain groups i.e., people with disabilities and pensioners employed, the rates may be different.

2.4.3. Solidarity tax

If the employee's income exceeds the maximum amount of social contributions, the employer and the employee is obliged to pay a solidarity tax on income above the stated maximum amount. The tax is calculated in accordance with the rates

stipulated by the Law "On State Social Insurance". In general, the employer rate is 23.59% and employee rate is 10.5%.

2.4.4 Sample of tax calculation from employment income

An employee without dependents who is a subject to all social insurance cases with the monthly salary of 1 000 euro and a non-taxable income is 75 euro.

1. Employee's social security payment
- 105 EUR (1 000 x 10.5%)
2. Payroll tax - 188.60 EUR
(1 000 - 75 - 105) x 23%)
3. Net employee's salary - 706.40 EUR
(1 000 - 105 - 188.60)
4. Employer's social security payment
- 235.90 EUR (1 000 x 23.59%).

3. Taxes

3.1 Corporate income tax and withholding tax on income of non-residents

Corporate income tax rate is 15%. Certain shipping companies may be taxed in accordance with the procedure set out for the tonnage taxpayers.

Taxpayer's taxable income is determined on the basis of the profit or loss before taxes indicated in the profit and loss account which is adjusted in accordance with the provisions of the Law "On Corporate Income Tax" (CIT Law).

3.1.1 Depreciation of fixed assets for tax purposes

According to the CIT Law taxpayer's taxable income shall be increased by depreciation of fixed assets and depreciation of intangible assets calculated in the financial accounting but decreasing by depreciation and write off amount calculated as per following CIT Law rates:

Category	Rate
Building, structures, permanent greenery	10%
Railway rolling stock and technological equipment, marine and inland navigation craft, technological fleet and port equipment, energy equipment	20%
Computing equipment and facilities, including printers, information systems, computer software systems, and data storage systems, communication equipment, photocopiers and their facilities	70%
Other fixed assets, except fixed assets mentioned under category 5	40%
Oil trial and extraction platforms and its equipment necessary for functioning located on these platforms, oil extraction and trial vessels	15%
Passenger cars	30%

For new production technology equipment acquired or constructed and used by taxpayer for its operational activities, the amount of depreciation during taxation period is calculated by applying coefficient 1,5 to the acquisition cost of fixed assets.

A taxpayer is entitled to reduce CIT taxable income shall be increased by the multiplier of 3 for the following expenses:

- 1) of scientific staff or technical staff recruited for the research and development activities;
- 2) the amount of compensation for research services performed by the scientific institution established as per register of scientific institutions of the Ministry of Education and Science or scientific institution based in Member States or residing in European Economic Area with whom Latvia has concluded a convention on double taxation and tax fraud prevention that has entered into force and the research activities are directly related to the taxpayer's research and development activities;
- 3) the amount of compensation for the testing, certification and calibration services for development of new product or technology provided by the certification, testing and calibration institution accredited by the national accreditation body or equivalent body based in the Member State or residing in European Economic Area with whom Latvia has concluded a convention on double taxation and tax fraud prevention that has entered into force.

3.1.2 Non-operational and representation expenses

Expenses that are not related to operational activities, as well as the amount of loss due to the maintenance of the social infrastructure facilities. Taxable income shall be calculated increased by the multiplier of 1.5.

Representation expenses up to 40% may be justified for operational activities and calculations of CIT.

3.1.3 Cars used for representation

Expenses related to representative cars with purchase value above 50 000 euro excluding VAT (including rent and interest payments), maintenance and usage are not deductible for the purposes of determining taxable income of CIT.

3.1.4 Tax loss transfer

Tax losses incurred before year 2007 can be used for 8 years (incl. year 2015). Losses incurred after 2007 can be used for an unlimited period of time. Companies registered in the special eligible areas for assistance may transfer tax loss incurred as of year 2005 with no time limit.

3.1.5 Doubtful and bad debts

When determining the taxable income, it may be reduced by the amount of bad debts if the criteria mentioned under the CIT Law are met. It includes the income related to debts having prior inclusion of the calculation of taxable income, the debt amount is written off from the amount of special savings or from direct losses (expenditure) of the taxable person in the accounts for the current tax period or in the previous tax periods etc.

3.1.6 Activities with shares and securities

CIT is not payable on income from sales of the EU or EEA publicly traded securities other than shares. While losses incurred on the sale of shares and the EU / EEA publicly traded securities are not deductible. Expenses related to acquisition, disposal or storage of stock and the EU / EEA publicly traded securities are not deductible.

3.1.7 The amount of deductible interest payments

The CIT law provides a restriction of deductible interest amount.

The taxpayer's taxable income has to be increased by higher of the amounts calculated as per following two methods:

Method 1 determines that taxable income shall be increased by interest payments (including discount rate) exceeding the amount of interest i.e., year's weighted average credit rate with 1.57 times increase for loans granted during taxation period to non-financial domestic enterprises using statistical indicators of the monetary financial institutions published in the website of the Bank of Latvia within one month after the end of the tax period.

Method 2 provides that taxable income shall be increased by interest payments proportionally the extent of loan obligations within the taxation period (interest rate calculated) whereas the average volume exceeds the amount which is equal to four times the amount of equity (at the beginning of the taxation period) as reflected in the taxpayer's annual report and reduced by long-term investment revaluation surplus and other reserves which are not incurred due to profit-sharing.

Interest payment included in the operational expenses may not exceed the amount of interest calculated according to the methods described above.

3.1.8 Tax from payments of non-resident legal entities (WHT)

Tax applies for the taxpayers in Latvia making certain payments to non-residents as per categories set in legislation. Taxable payment groups and the applicable rates are available in the table below.

The tax rate can be reduced on the basis of exemptions provided in the tax conventions. Latvia has signed convention with number of countries; a list of it is available in the sub-section 3.1.9.

15% tax shall be withheld from all payments to low or tax free countries / territories except payments for the goods purchased at market prices or payments for publicly traded securities purchased in the EU or the EEA if they are purchased at market prices.

Payment	Rate
Dividends (1)	0%/15%/30%
Management and consulting services (2)	10%/15%
Interest payment (3)	0%/15%/5%
Payment for intellectual property (3)	0%/15%
Payment for using movable property and real estate (4)	0%/5%/15%
Compensation for sale of real estate or sale of shares (5)	2%/15%

Notes:

(1) As of 1 January 2013, the CIT Law exempts WHT on dividends, except payment to countries with low tax or duty free countries / territories residents. In such case, standard tax rate is 15% or an extraordinary (interim) dividend rate is 30%.

(2) 10% tax should be withheld on payments for management and consulting services. WHT rate can be reduced by applying exemptions as per tax conventions unless services are provided by permanent establishment in Latvia. A 15% WHT applies to all payments made to residents of countries/territories with low tax or duty free tax regime.

(3) As of 1 January 2014, the CIT Law exempts WHT on specific payments to non-residents, except if the payment is made to residents of low tax or duty free countries / territory. In this case, 15% WHT applies. 5% WHT applies if interest payments are made by Latvian credit institution to a resident of low tax or duty free countries/territories.

(4) Payments to residents of low tax or duty free countries are subject to 15% WHT, for the rest 5% WHT applies. As of 1 July 2013, WHT exemption applies on payments for the right to use manufacturing, commercial or scientific equipment or for its utilization (except payments to residents of low tax or duty free countries.

5) Income from share of the capital or share disposal or company in Latvia or company registered abroad or other person if more than 50% of the value of the assets directly or indirectly (due to participation of one or more of other persons in Latvia or registered persons abroad) forms real estate in Latvia. It does not apply to income due to disposal of publicly traded securities from EU or EEA.

3.1.9 Tax conventions

Latvia has tax conventions in force with the following countries since 2015:

Albania	Germany	Macedonia	Slovenia
Armenia	Greece	Malta	Spain
Austria	Georgia	Mexico	Sweden
Azerbaijan	Hungary	Moldova	Switzerland
Belarus	India	Montenegro	Tajikistan
Belgium	Ireland	Morocco	Turkey
Bulgaria	Island	the Netherlands	Turkmenistan
Canada	Israel	Norway	Ukraine
China	Italy	Poland	United Arab Emirates
Croatia	Kazakhstan	Portugal	United Kingdom
Czech Republic	Korea	Rumania	USA
Denmark	Kuwait	Russia	Uzbekistan
Estonia	Kyrgyzstan	Serbia	Qatar
Finland	Lithuania	Singapore	
France	Luxemburg	Slovakia	

3.1.10 List of low tax countries and territories

68 countries and territories are included in the list of low tax countries / territories i.e., Andorra, Anguilla (Great Britain and Northern Ireland) etc. in 2015. The full list is available in the Cabinet of Ministers Regulations No. 276 "Regulations on the low-tax or tax-free countries or territories."

3.1.11 Transfer pricing documentation

The taxpayers are obliged to justify that transaction price corresponds to the market price (value) if they perform transactions with related parties. If taxpayer's net sales for the reporting year exceed 1 430 000 euro and the amount of the transaction with related parties exceed 14 300 euro. Information stated as per the Law "On Taxes and Fees" has to be described in the relevant documentation.

3.2 Micro enterprise tax

Taxpayers can choose to pay the micro enterprise tax instead of the corporate income tax if they comply with the statutory criteria of the Law of Micro business tax, including the turnover of the calendar year not exceeding 100 000 euro. Micro enterprise tax shall be paid based on the turnover of calendar year at the rate of 9%, but starting from the fourth year operating as rate of micro enterprise tax is 12%. Minimum amount of micro enterprise tax for a year is 50 euro.

As of 2017 micro enterprise will not be entitled to choose to pay the micro enterprise tax if it carries out operational activities in the sectors stated in the Cabinet Regulations No. 540 "Regulations on the sectors where the micro enterprise

tax regime does not apply." There are 37 industries in the list i.e., logging, metal production, building construction, wholesale, computer programming, legal and accounting services, architectural services, advertising, market research and other professional, scientific and technical services, recruitment and others.

Besides corporate income tax, micro enterprise tax covers a micro business owner's personal income tax on part of its revenue, mandatory national social insurance contributions, personal income tax and business risk duty for a micro business's employees.

From 2017 employees of micro enterprise will be required to pay national social insurance contributions.

3.3 Personal income tax

Personal income tax at rate of 23% applies on employment income and income from operational activities in Latvia. For other types of income there are following tax rates applied:

- income from capital for example, real estate, shares, intellectual property objects -10%
- income from increase of capital - 15%

- dividends - 10%
- interest or similar income - 10%
- income from private pension funds and life insurance contracts with accumulation of funds - 10%.

3.4 Value added tax (VAT)

3.4.1 Rates

Standard rate of VAT is 21%; reduced VAT rates are 0% and 12%.

Zero rated VAT is applied on the following:

- export, services relating to the import, export, transit
- supplies of non-Community goods in customs warehouses and free zones
- ship and aircraft supplies, repair
- supplies of goods to the VAT payer registered in other Member State
- import of goods if goods unaltered are supplied within 30 days to the taxpayer registered in Member State
- supplies of new vehicles to any person in Member States
- supplies of goods and services rendered to diplomatic and consular missions, international

- organizations, the European Union institutions and the North Atlantic Treaty Organization (NATO)
- other.

The reduced rate is 12% which applies to medicines, medical equipment, special food for infants, training and original literature, newspapers, magazines, tourist accommodation, wood and heat supply for household consumption.

3.4.2 VAT exempt transactions

VAT exempt applies for certain postal services provided by the universal postal service, medical and dental services, social welfare, vocational and social rehabilitation, pre-school education provided by the children's residence and pre-school services, a state-recognized education services in general education, vocational education, higher education and interests in the field of education, certain cultural services and other transactions as per Article 52 of the VAT law.

3.4.3 Optional provisions of VAT Directive¹

The following optional provisions of the VAT Directive are implemented in Latvia:

1. Council Directive 2006/112/EC of 28 November 2006 on the common system of value added tax

- VAT group
- VAT exempt on services by members of an independent group
- special scheme for imports of goods
- reduction of the tax payable on the taxable amount of bad debt
- the reverse of the VAT scheme applicable to domestic transactions for timber, scrap metal and building services (as of 1 April 2016 also for mobile phone, tablet, laptop and integrated circuit devices domestic supplies)
- option to apply the tax on sale of used real estate.

3.4.4 Restrictions of input VAT deduction

From the amount of tax due to the state budget is not deductible as input tax paid for the following goods or services:

- unused goods and services for the purposes of taxable supplies
- costs of representation car with value over EUR 50 000 excluding VAT, as well as costs of it maintenance including repair and purchase of fuel
- 60% of the tax on the representation costs for purchased goods and services related to the public conferences, receptions and

- organization of meal, as well as representation materials produced for representation purposes by tax payers registered
- 50% of the tax on the purchase, leasing or import of passenger vehicle with no more than eight seats, excluding the driver's seat, as well as vehicles' maintenance costs i.e., vehicles repair and purchase of fuel².

3.5 Other taxes

3.5.1 Car operation tax

In Latvia, the tax is paid by all persons who have registered or are registered taxable car owned, hold or controlled even if vehicle registration plate is issued for transit purpose. The car circulation tax is imposed on all vehicles except tractors, automobile trailers and semi-trailers with laden mass below 3 500 kg, trams, trolley-buses, off-road vehicles, snow bike, mopeds and bicycles.

The amount of the tax for motorcycles, three and four wheeled motorcycles, depends on the engine capacity and from 17.07 to 68.30 euro. Cars circulation tax is calculated by summing the rates according to gross vehicle weight, capacity and maximum power of engine.

With regard to vehicle without engine technology in the design, buses and lorries, the tax is calculated according to its weight. Tax amount is from 17.07 to 256.12 euro.

3.5.2 Tax on company cars

Company car tax is paid by companies which use passenger cars and commercial vehicles (mentioned below) simultaneously for both business and private purposes. Tax exempt applies on vehicles registered for use of business purposes only as per law.

Company car tax is applied to the merchant, farm, branch of a foreign company owning or holding registered vehicle or on the basis of employment contract or from a person who is not economic operator or branch of a foreign company or a farm, lending the following:

- 1) passenger cars (except when the lending of vehicle is used for economic activity less than 15 days during a calendar month)
- 2) Commercial vehicles with laden mass up to 3 000 kg registered as vans and having more than three seats including the driver's seat in force as of 1 January 2016.

2. It does not apply to cases where the vehicle is used for the purpose to provide passenger transportation services, car rental services, hire-purchase services or are used in trade of vehicles, transport services, and in other cases as stated in the VAT Law

Passenger cars are considered due to its construction and interior equipment intended for carriage of passengers and their baggage and comprising eight seats in addition to the driver's seat registered as passenger cars or cars multi-purpose use in the Register.

If the vehicle is registered after 1 January 2005, the tax rate is of 29 euro/per month to 62 euro/per month depending on the vehicle's engine capacity. If the vehicle is registered before 1 January 2005, it is 46 euro/per month³.

3.5.3 Real estate tax and state duty for registration of real estate

The real estate tax is paid by companies in Latvia and foreign enterprises and natural persons owning or possessing real estate i.e., land, buildings and civil engineering structures in Latvia.

The real estate tax rate ranges from 0.2 to 3% of the cadastral value of the property. Rates are set according to each local government provision issued by the 1st of November year before. In some cases, the local government has the right to impose increased tax rate.

When selling real estate, the buyer of the real estate has to pay a state fee. The fee is 2% of

the highest: the purchase or the cadastral value of the property. The duty rate of 6% is applied in case the property is purchased by a legal person who performs business activities. The maximum amount of the fee if the property does not contain any residential buildings is 42 686.15 euro. The duty rate is 0.5% that applies on the value of real estate if the ownership is transferred to the relatives i.e., children, spouses, parents, sisters, brothers, grandparents, grandchildren.

3.5.4 Environmental tax

Environmental tax applies to legal and natural persons who:

- 1) have received or were obliged to receive the authorization, license or certificate for category C polluting operations for:
 - acquiring natural resources taxable
 - selling taxable natural resources acquired not classified as mining and quarrying
 - utilize underground natural resources by deep injection of natural gas of geological areas or greenhouse gases emissions
 - releases taxable polluting substances in the water and air
 - dispose waste in landfills and dumps
 - releases greenhouse gases from fixed

technological equipment

- use water resources for electricity generation in hydro power plants with hydroelectric capacity less than two megawatts
- utilize radioactive substances which produce waste that need to be stored or disposed in the territory of the Republic of Latvia.

2) the first in Latvia:

- sell environmentally harmful goods, coal, coke and lignite (brown coal), fireworks
- sell packaged goods, add package to the packaged goods or unpackaged products for the buyer's convenience or advertising
- use environmentally harmful goods or goods purchased in packages, except goods taxable upon selling
- add packaging to the product or services sold to the recipient
- use coal, coke and lignite (brown coal) and fireworks for the purpose of ensuring own economic activities

3) sell of disposable tableware and accessories made of plastic, paper, cardboard, laminates of polymer or metal components and metal foil for catering and retailing services in Latvia

4) continually register vehicles covered by Law on Out of Use Vehicle Statutory Management.

Taxable objects, applicable tax rates and tax exemptions are governed by the Natural Resources Tax Law.

3.5.5 Excise tax

In Latvia excise tax is applicable on alcoholic beverages including beer, tobacco products, petroleum products, coffee, soft drinks and natural gas.

Excise tax is applied regardless of whether the excise goods produced in Latvia, imported from third countries or imported from other EU Member States.

Special permit (license) for performing commercial activities with goods subject to excise tax must be obtained including wholesale of alcoholic beverages, tobacco products or trade of fuel, retail sale of alcoholic beverages, beer, tobacco products or fuel, certified warehouse operations, registered beneficiary for operation with alcoholic beverages, tobacco products or oil products, registered shipper operation with alcoholic beverages, tobacco or oil products.

3.5.6 Electricity tax

Electricity tax is applied on the electricity supplied to the end user as well as the electricity generated and delivered for own consumption.

Electricity tax payers are persons who supply electricity to end-users, including:

- licensed electricity producers
- licensed distribution system operators
- licensed electricity traders
- autonomous electricity producers, except autonomous producers who generate and consume electricity for their own use, provided that the total production capacity of up to two megawatts, and energy products, which is subject to excise duty, coal taxable with the nature resource tax or electricity taxable electricity tax
- Electricity end-users, if there is a contract or other agreement for the purchase of electricity stock exchange.

3.5.7 Lottery and Gambling Tax

Lotteries and gambling tax is paid by the legal entities that have received a special permit (license) to organization of lottery and gambling and its maintenance as per legislation.

A state duty is charged for a special permit (license) for the gambling organization and maintenance. The annual re-registration of special permit (license) has to be arranged starting from the next year following issuing or renewal. State fee for receiving permit (license) to open the casino, gambling and bingo halls shall be paid prior receipt of the permit (license) or before the date of issuing the permit (license).

Authorization to organize lottery of goods or services, a merchant who manufactures, distributes, sells goods and services has to apply for lottery permit in Lottery and Gambling Supervisory Inspection of the Ministry of Finance.

If prize fund does not exceed 720 euro, a lottery of goods or services can be arranged without permit and duty free.



4. Investment initiatives

The following tax incentives have been implemented in view of foreign investment in Latvia:

- Corporate income tax (CIT) discount on long-term investments exceeding EUR 10 million. Tax credit of 25% for investments of less than 50 million euro and 15% for investments over 50 million euro
- CIT and property tax relief for companies registered in the special economic zone or free port
- CIT relief to agricultural enterprises.



5. Permits and licenses

Number of sectors and upcoming economic activities i.e., transport of goods and passengers, pharmaceutical wholesale and retail, waste management require a permit and special licenses. The building company must register at the Construction merchant register etc.



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6. Useful
information

6. Useful information

For more detailed information on the laws to be applied, registration of economic activities in Latvia and procedures of receipt of permits and licenses can be found in the websites of the following state institutions:

Ministry of Finance: www.fm.gov.lv

State Revenue Service: www.vid.gov.lv

Register of Enterprises: www.ur.gov.lv

Investment and Development Agency of Latvia:
www.liaa.gov.lv/en

Ministry of Economics: www.em.gov.lv

Treasury of Republic of Latvia: www.kase.gov.lv